

# OVERSIGHT OF THE U.S. SECURITIES AND EXCHANGE COMMISSION

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## HEARING

BEFORE THE

## COMMITTEE ON

## BANKING, HOUSING, AND URBAN AFFAIRS

## UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

SECOND SESSION

ON

EXAMINING THE WORK AND AGENDA OF THE U.S. SECURITIES  
EXCHANGE COMMISSION

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JUNE 14, 2016

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TUESDAY, JUNE 14, 2016

U.S. SENATE,  
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,  
*Washington, DC.*

The Committee met at 9 a.m., in room SD-538, Dirksen Senate Office Building, Hon. Richard C. Shelby, Chairman of the Committee, presiding.

### OPENING STATEMENT OF CHAIRMAN RICHARD C. SHELBY

Chairman SHELBY. The Committee will come to order.

This morning we will receive testimony from Securities and Exchange Commission Chair Mary Jo White. Oversight of the Commission is an important part of this Committee's jurisdiction.

The SEC is an independent agency tasked with protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation.

The SEC is responsible for ensuring transparency so that investors have adequate information to make investment decisions and to mitigate conflicts of interest, fraud, and manipulation.

This regulatory paradigm is one reason why our capital markets have long been the envy of the world and the lifeblood of our economy. Excessive and unnecessary regulation, however, may endanger America's status as the world's preferred financial center.

First and foremost, I believe the SEC should focus on its core mission. This has become more difficult as the Commission has come under increased pressure to expand its mission and cater to special interests.

Examples of such efforts include attempts to force the SEC to mandate disclosure on climate change and political contributions. These efforts are not new, and the SEC has withstood political pressure in the past. It is my expectation that it will continue to do so in the future.

Chair White, as you pointed out in a 2013 speech, and I will quote you, ". . . we make our decisions based on an impartial assessment of the law and the facts and what we believe will further our mission—and never in response to political pressure, lobbying, or even public clamor."

The SEC must, I believe, continue to adhere to those principles and uphold its fundamental mission. It should also periodically review the appropriateness of its existing rules.

For example, while the Commission has undertaken work to review equity market structure, it has not engaged in a comprehen-

sive review of its rules, even in light of the so-called Flash Crash, which happened over 6 years ago.

I also hope that the SEC will continue to take very seriously the importance of strong economic analysis when promulgating rules.

As we have seen, agencies that fail to undertake such an analysis in their rulemakings are vulnerable to legal challenges, as well they should be.

An agency with thousands of employees like the SEC should be able to analyze in detail the impact of its rules on the markets, investors, financial products, and the broader economy.

This is especially true today, given the cumulative impact and unintended consequences of the myriad new rules stemming from the financial crisis.

If the cost of a rule outweighs its benefit, then the rule should be eliminated. If a rule passes cost/benefit muster, it should then be implemented by the appropriate agency.

The SEC has the primary expertise in capital markets and should be the lead agency in regulating them. Specifically, I am concerned that attempts by other Federal agencies to erode, Madam Chair, the SEC's jurisdiction could undermine the integrity and functioning of these markets.

Recent examples of this include the Department of Labor's fiduciary duty rule, the FSOC's continued focus on asset managers, and the Federal Reserve's targeting of broker-dealers under the guise of reining in what it calls "shadow banking."

The SEC has eight decades of specific expertise in these matters. This should outweigh the desires of other regulators to expand their powers at the expense of investors and the markets.

Chair White, I look forward to hearing your thoughts on these issues and the future agenda of the SEC.

Senator Brown.

#### **STATEMENT OF SENATOR SHERROD BROWN**

Senator BROWN. Thank you, Mr. Chairman, and welcome, Madam Chair. Good to see you again.

Over 3 years ago, you were confirmed as Chair of the SEC and assumed the task of guiding the Commission's significant rule-making agenda under the Wall Street Reform Act and the JOBS Act. At that time the destruction of \$13 trillion in household wealth from the financial crisis was still fresh in our minds. The SEC and other financial regulators had completed many of the Wall Street reform rulemakings and were evaluating how to finish the implementation of the rest.

When you last appeared before this Committee in September 2014, you said the staff was proceeding on the outstanding rules, we could expect to see additional rules shortly. Although several rules have been proposed and some finalized, many are still incomplete. In particular, the Commission has not finished the derivatives rules under Title VII of the Wall Street Reform Act, and the path to their completion seems unclear. These rules are important because Title VII is a key part of reform to the financial markets.

By increasing transparency, by enhancing oversight, by moving to more resilient and stable trading platforms, Congress wanted to make sure that future crises could be detected sooner and would

do less damage. This is not entirely on your shoulders, on the SEC's shoulders, but there are certain markets, such as credit default swaps, that depend on SEC. Until the rules are completed, the SEC and other regulators will not have the benefit of a framework that provides transparency and access to market data.

Another Wall Street Reform Act rule that remains outstanding would prohibit incentive compensation that could lead to excessive risk taking or significant losses at financial firms. We know what happened during the financial crisis in that regard.

The multiagency rule was proposed in 2011 and repropoed last month. Six years after Wall Street reform became law, this rule still is not finished.

The final rule would provide the market and the public with some assurance that senior executives at financial institutions will not be rewarded for taking inappropriate risks that could harm the markets, could harm their employees, or could harm the economy. I urge you and other regulators to finish that rule as quickly as possible.

During your confirmation hearing, you stated that you would make strengthening enforcement a high priority throughout your tenure. You said then, and I agree, that "investors and market participants need to know that the playing field of our markets is level and that wrongdoers, individual and institutional, of whatever position or size, will be aggressively and successfully called to account by the SEC." Yet time and again, we see repeat offenders enter into settlement after settlement that seem to have no effect on stopping the problem in the first place.

As the cop on the beat, the question is: At what point is the SEC going to stop handing out warnings and start giving tickets?

This is evidence in the waiver process. SEC has routinely granted waivers to banks following a variety of violations that could have resulted in the loss of certain privileges under security laws. Unfortunately, granting those waivers eliminates the significant consequences that could promote better overall compliance at those institutions.

Finally, I would like to return to an issue that has been discussed many times in this Committee. Democrats in the Senate have repeatedly asked you to begin work on a corporate political spending disclosure rule. This is not a plea from a special interest, as some on the other side of the aisle might say. This is good Government policy. When you were last here, you acknowledged the "intense interest of investors and others" on this issue, but you pointed to the low priority of mandatory rulemaking. I realize this year's appropriations bill limits the SEC's work on that rule, but it should not prevent you from doing anything at all.

I sincerely hope you begin work on a corporate political spending disclosure rule. The interest in it has only become more intense. I am interested in hearing your update, Madam Chair.

Thank you.

Chairman SHELBY. Madam Chair, your written testimony in its entirety will be made part of the hearing record. You have been here many times. You proceed as you wish.

**STATEMENT OF MARY JO WHITE, CHAIR, SECURITIES AND  
EXCHANGE COMMISSION**

Ms. WHITE. Thank you, Mr. Chairman, Ranking Member Brown, and other Members of the Committee. Let me, before I start, just express—I am sure I speak for everyone—that my thoughts and prayers are with the victims of the Orlando shootings and their families.

Thank you for inviting me to testify today on the current work and initiatives of the SEC, which are, as the Chairman indicated, summarized in some detail in my written testimony.

As you know, the SEC is a critical agency that is charged with protecting millions of investors and safeguarding the most vibrant markets in the world. And the Commission has been very busy since I last testified before the Committee in 2014. The last 3 years have each been marked by a vigorous enforcement and examination program, empowered with new tools and methods to protect investors and hold wrongdoers accountable. In fiscal year 2015 alone, the Commission brought over 800 enforcement actions, an unprecedented number; secured over \$4 billion in orders directing the payment of penalties and disgorgement, an all-time high; performed approximately 2,000 exams, a 4-year high; and, even more importantly, continued to develop cutting-edge cases and smarter, more efficient exams.

The strength of our enforcement program can also be seen in the kinds, complexity, and importance of the cases we bring that span the securities industry, include numerous first-of-their-kind actions, and focus heightened attention on market gatekeepers like ATSS, exchanges, accountants, and lawyers.

Significantly, approximately two-thirds of our substantive actions in fiscal year 2015 also involved charges against individuals, and we continue to obtain admissions in certain cases, which we have now done in over 50 instances since we changed our settlement protocol.

The Commission over the last 3 years has also pursued very consequential rules and other initiatives to protect investors, strengthen markets, and open new avenues for capital raising. Since I last testified, we, for example, advanced major rules addressing key equity market structure issues—including controls on the technology used by key market participants, the transparency of alternative trading systems, and the consolidated audit trail—while moving forward with a broader assessment of other fundamental changes. We issued a series of proposals to address the increasingly complex portfolios and operations of mutual funds and exchange-traded funds. We adopted new rules for crowdfunding and smaller securities offerings under Regulation A, while also proposing additional avenues for small businesses to raise capital. We finalized major components of the regulatory regime for security-based swaps, and we continued to execute a comprehensive review of the effectiveness of our disclosure regime.

This work marks the latest phase of extraordinary regulatory efforts by the agency both before and after I became Chair, enlisting all of our policy divisions and offices. Beyond our discretionary initiatives, the Commission has now adopted final rules for 66 of the mandatory rulemakings of the Dodd-Frank Act, the majority of

them since I became Chair. And, Senator Brown, Title VII is a major priority for 2016, which I am sure we will get into. We have also now completed all of the rulemakings directed by the JOBS Act, and we have made significant progress on the rulemakings required of us late last year under the FAST Act.

While our work in enforcement and rulemaking are perhaps the most prominent examples of the agency's achievements, the imperatives of our mission are also carried forward each day by the dedicated staff of our divisions and offices.

The Division of Corporation Finance reviews the annual and periodic reports of thousands of issuers each year, helping to ensure that investors receive full and fair disclosure about the public companies in which they invest.

Last year, the Division of Trading and Markets reviewed more than 2,100 filings from exchanges and other self-regulatory organizations to preserve a fair and orderly marketplace for all investors.

The Division of Investment Management reviewed filings last year covering more than 12,500 mutual funds and other investment companies, where many individuals, as you know, invest their hard-earned money to save for retirement, college, and other important goals.

Our economists in the Division of Economic and Risk Analysis produced more than 30 incisive papers and publications in 2015, including two major analyses to help inform our work on asset management.

This afternoon, I will actually have the privilege to participate in our annual awards ceremony at the Commission where we recognize some of the tremendous work of some of our staff.

The Commission today is a stronger and more effective agency, and I am honored to lead the agency during this time. Nevertheless, significant challenges remain if we are to address the growing size and complexity of the securities markets. It is critical that the SEC has the resources required to discharge our responsibilities, the new ones and the many others we have long held, in the face of a growing and ever more sophisticated financial services industry.

I deeply appreciate that we must be prudent stewards of the funds we are appropriated, and we strive to demonstrate how seriously we take that obligation by the work that we do. At the same time, our resources are insufficient, and the cuts and limitations to the SEC's budget that the House bill proposes would seriously imperil the progress we have made and diminish our ability to fulfill our mission.

While more remains to be done and achieved, I am very proud of the agency's impressive accomplishments across the range of its responsibilities. For that I want to again thank, first and foremost, the exceptional staff of the SEC as well as my fellow Commissioners, present and past. And I want to thank the Chairman, the Ranking Member, and this Committee as a whole for your support. Your continued support will allow us to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and build on the significant work we are doing.

Thank you very much. I am happy to take your questions.

Chairman SHELBY. Thank you.

Madam Chairman, I understand that the Commission can vote to delegate certain of its authorities to the SEC staff, including enforcement proceedings. Once the Commission has voted to delegate, how are you and your fellow Commissioners at the Securities and Exchange Commission made aware of the staff's use of that authority? And if the Chair is recused on a specific matter, who is accountable for the staff's use of the delegated authority?

Ms. WHITE. The Exchange Act actually is explicit on this, Mr. Chairman, that the Commission as a commission has the authority to delegate many of its day-to-day functions. It does not have the power, for example, to delegate rulemaking to the staff or—

Chairman SHELBY. That is set out statutorily?

Ms. WHITE. Yes, it is statutorily done.

Chairman SHELBY. OK.

Ms. WHITE. There are hundreds and hundreds of day-to-day things that we must do at the Commission, so it is very important that the staff have delegated authority to act.

As safeguards, however, on that delegated authority, the Commission can review any of those actions. The staff itself can decide to refer something to the Commission even though it may have delegated authority from the Commission to decide. And the review of the Commission can be precipitated by any one Commissioner's desire to do so.

Chairman SHELBY. Once the Commission votes to delegate its authority to the staff, it is my understanding that such delegation remains in place under future Commissions, and new Commissioners do not have a chance to approve existing delegations of authority. Is that correct?

Ms. WHITE. Yes, it is, Mr. Chairman. I think essentially the way it works is that if one wanted to review or change a delegation, it would be up to the Chairman to put that on the agenda, whoever the Chairman is.

Chairman SHELBY. Madam Chair, would you support an SEC review of existing delegations, including an analysis of their appropriateness? In other words, you look back—you do oversight, I hope, in your agency, like we do here. Is it not important to look back and see what—

Ms. WHITE. Since I have been there, it is certainly something that I have discussed with various of my fellow Commissioners, and we all have the list of delegations that exist. I have urged my fellow Commissioners, if they have an issue with any particular delegation, to bring that to my attention, and we will certainly look at it.

Chairman SHELBY. You have often stated, Madam Chair, that the Securities and Exchange Commission is an independent agency. That is the way we want it to be. It was set up that way. And while one can expect some split votes because of the way the Commission is set up, there have been many party-line 3-2 and 2-1 votes under your chairmanship. By comparison, according to the press, former Chairman Richard Breeden never had a 3-2 vote, and former Chairman Levitt rarely would take a matter to a vote unless he knew he had a 5-0 vote.

Are there any areas that you can work on cooperatively with the other two Commissioners to reach a unanimous decision? And if so, could you give us some examples?

Ms. WHITE. I think we certainly strive for consensus——

Chairman SHELBY. We know everything is not unanimous.

Ms. WHITE. Everything is definitely not unanimous. I think somebody gave me a figure the other day that about 65 to 70 percent of our votes are actually unanimous. But, obviously, that is still a percentage that have not been unanimous. I think I have discussed with you, Mr. Chairman, and I think Senator Brown and probably some of the other Members of the Committee as well, that one thing that I have found as Chair, even though we strive for that consensus—unanimity, indeed—on all of our rulemakings, so many of our mandated rulemakings have been under the Dodd-Frank Act, and the controversies surrounding the act at the time it was adopted have continued into the implementation of those rules. So we have ended up with an extra challenge reaching consensus because of that.

Chairman SHELBY. Madam Chair, in 2013, you posed for comment a study on assessment management by the Office of Financial Research that was requested by FSOC. This allowed the public a meaningful opportunity to provide feedback on the study and highlighted significant flaws.

Given the benefit of public comments on that study, will you commit to posting other FSOC-requested studies affecting SEC-regulated entities? And if not, why not?

Ms. WHITE. Well, I think certainly at the SEC, and I think at other agencies as well, the benefit of the notice and comment process and even just a comment process if you are not in an APA rulemaking, is enormous. So I think getting that feedback is important. The report that you referenced, Mr. Chairman, was actually the report of OFR. They publicized it. But we did open a comment window because we thought it was important to gather public input in one place. If we were in another situation like that and OFR or FSOC itself did not post its studies to make it easier for the public to comment, certainly we would seriously consider that again.

Chairman SHELBY. My last question is in the area of repeated violations. There have been concerns raised by the public as well as Members of this Committee about repeated violations by SEC-registered entities. Two years ago, a former SEC Commissioner stated with respect to the most egregious and repeated violations of our securities laws and regulations, and I will quote, “We need to ask ourselves a fundamental question: Should the violating entity retain the privilege of participating in our capital markets?”

My question to you is this: In your opinion, when is it appropriate for the SEC to exercise its ability to deregister an entity? And if you could give us an example, that would help.

Ms. WHITE. I think it is an enormously important power that we have and should wield in appropriate circumstances to police the markets——

Chairman SHELBY. It goes to the integrity of the market.

Ms. WHITE. Absolutely right. Absolutely right. I think you have to look very carefully at what the violations have been over what period of time, and who was involved in them. You want an aggres-

sive enforcement program to bring cases when they are there to bring. I am certainly quite open in the interest of strong protection of our markets that there comes a point where one of our regulated entities should no longer be registered, and I would not hesitate to bring a proceeding to revoke the license.

Chairman SHELBY. Thank you.

Senator Brown.

Senator BROWN. Thank you, Mr. Chairman.

Some of my colleagues—there seems to be a sort of collective amnesia on this panel in some cases and in this body about what happened with the financial crisis since some of my colleagues as a result, particularly in the House but some here, continue to push for the repeal of the Wall Street Reform Act, insisting it has created more problems in the financial system than it has prevented. A couple of questions to start with.

Are you concerned by efforts to repeal Wall Street reform? Do you think it has been effective in improving our financial stability?

Ms. WHITE. I think the reforms under the Dodd-Frank Act have been enormously important in strengthening our financial system. Collectively, I think our financial system is much stronger and resilient now, certainly in part because of the actions undertaken by Dodd-Frank. So I certainly would not want to see those reforms repealed.

Senator BROWN. OK. Thank you. Despite the improvements to date that you have mentioned and that are self-evident with a stronger, more stable financial system, this reform, of course, is still a work in progress. In my opening statement, I mentioned the derivatives rules that are still outstanding. I am not just concerned that it is taking the SEC so long to finish its rules, but also that SEC is far behind other agencies implementing rules in similar issue areas. Let me give two examples.

The CFTC covers a much larger portion of the derivatives market and has made significantly more progress than has SEC, even accounting for a few hiccups along the way, with far fewer resources than you have.

Second, the Department of Labor was able to propose and repropose and finalize its fiduciary rule while the SEC only produced a study called for by the Wall Street Reform Act.

In neither of those cases was the process perfect, of course, nor is our final rules perfect, but both agencies were able to adapt along the way and move forward. Why is the SEC slower than those agencies? What is not working?

Ms. WHITE. I think considering what the SEC was given between the Dodd-Frank Act and the JOBS Act, plus obviously all of our various “discretionary responsibilities,” which are vast, we have undertaken in the last few years a historic level of regulatory activity of great complexity. And I think I have said this before about Dodd-Frank and the JOBS Act in particular, and I have said it from the day I arrived, I am deeply committed to getting the congressional mandates under both of those statutes, and now the FAST Act, done as promptly as I can, but they need to be done well, and they need to last, and they need to be adaptable to how our markets change.

I think with respect to the other issue you mentioned—the Department of Labor fiduciary duty rule—that is an authority that Dodd-Frank gave the Commission to decide whether to exercise or not. It is not a statutory mandate.

Now, I have said myself, speaking for myself, about a year ago after extensive study that I think there should be a uniform fiduciary duty rule coming from the SEC under Section 913 of the Dodd-Frank Act. That is speaking for myself. The staff has proceeded to develop outlines of recommendations, but it is up to the Commission as a whole to decide whether to advance that rule and then what its parameters should be.

In terms of Title VII and the derivatives markets, you are right, our share of that market is a little less than 5 percent, but it is an important part of those markets. Again, before I arrived—and this is not meant by way of criticism at all; I see how it made sense—what the SEC decided to do with its Title VII rulemakings is essentially publish a policy statement that set forth a sequence of when the SEC would adopt proposals first and then finalize those rules before they become effective. So we have been following that road map.

I think there could not be a higher priority among all of the Commissioners, the three of us there now and the other two that left us last year, than completing those Title VII rulemakings. And I think in terms of this regulatory year, that is a very high priority certainly to finalize. We have finalized a number of those rules since I was last here, but in terms of the reporting and the registration and regulatory mechanisms for dealers, I am hoping we are done with those by the end of this year.

Senator BROWN. Thank you. We know from during the financial crisis how important it is that regulators work together. Industry is good at shifting its business model to find gaps, to find areas of weakness in the regulatory structure. Congress for whatever reasons chose not to combine any of the financial agencies 6 years ago, obviously did FSOC, but beyond that not really combining these agencies, and it makes your cooperation with other agencies all that much more important.

Let me ask one other question. Democratic Members, Madam Chair, of this Committee and others have taken a close look at the policies and the practices and the decisions surrounding the waiver applications the SEC receives from financial institutions. I thank you and your staff for the information you have provided to us, to the Banking staff so far. I hope we can count on you and your team for additional assistance when needed as they make more requests.

Ms. WHITE. Absolutely. I think it is an enormously important area. As you know, Senator, it is an area that I focused on right at the outset of my tenure as Chair. We have made a number of changes to enhance the robustness of the process and the transparency of the process. Obviously, we continue to look at that for whether there are other enhancements that would make sense, particularly in the area of when we do not grant the waivers because we want to make certain that the public knows that there are many cases, including those involving financial institutions, where the waivers are not granted. But because of the nature of our process, that is not as transparent for reasons that are histor-

ical and good. You want to encourage people to come in and talk to the staff about whether they qualify or they do not, and often what they submit is nonpublic information. But I continue to look at that aspect of our process. I have certainly, since I became Chair, directed the staff to keep track of those instances that do come in and are not granted, assuming they are not anonymous, and, obviously, a number of people just will not apply for waivers because they know under our guidelines that they would be denied or would not be granted a waiver because of what the guidelines specify.

Senator BROWN. Thank you. We have particular concern about the lack of transparency in those waivers that are granted. The public sees an institution violates the law, asks for a waiver; the SEC issues a short notice approving the waiver. What do you do to—how can you assure us that the public and this Committee and everybody in our society will be able to understand more what has happened in how you bring more transparency when these waivers are granted?

Ms. WHITE. Well, again, on those that are granted, which I think are the ones you are addressing now, not those that are not granted, they are publicized on our Web site. They also are subject—in the case of the so-called WKSJ waivers and the bad-actor waivers and some of the other waivers as well to the public criteria that the staff or the Commission considers when reviewing those requests. And then what is published on our Web site really does march right through what those criteria are and the facts under each one.

Again, if there is some enhancement that would make sense, I am certainly open to considering it.

Senator BROWN. OK. We will come to you about that. Thank you.

Chairman SHELBY. Senator Crapo.

Senator CRAPO. Thank you, Mr. Chairman.

Chair White, modernizing our market structure is a complicated but necessary task, and I appreciate all the work that has been done by the SEC as well as by the market participants, investors, and academics on this issue.

Senator Warner and I held a subcommittee hearing on this topic in March, and one of the takeaways was that while there has been a lot of positive input and work done in this area, there is concern about the pace of reform efforts and what will be accomplished.

What are the top market structure objectives that you want to achieve this year? And how will this strengthen our markets and benefit investors?

Ms. WHITE. It is an enormously important area and, as you know, a very high priority for me personally, both in terms of some specific short-term reforms as well as a comprehensive review, soup-to-nuts, of the entire regulatory regime. We are building on, fortunately, I think the strongest, most reliable markets in the world, but that does not mean that they cannot be enhanced and optimized. So I have been pleased with the staff's work—but I always want things to be done sooner. That is my personality, among other things, and we certainly are concentrating a lot of resources on it. I have also been pleased to date with the work of the EMSAC—the Equity Market Structure Advisory Committee—that

we formed early in 2015. They are tackling the core issues. As you know, Senator, the committee has received a recommendation from one of its subcommittees about the possibility of doing a maker-taker pilot. That is obviously one of the core issues. We are expecting a telephonic meeting where the subcommittee is expected to make a specific recommendation on July 8th, so I look forward to that. I think that is a very important area.

A lot of things have actually already been done in the market structure arena. One is obviously in the area of resiliency of the markets. Shortly after I testified here in 2014, we adopted Regulation SCI, which is the Systems Compliance and Integrity rulemaking that is aimed right at the critical market infrastructures and enhancing their resiliency and responses to incidents when they occur. That rule is now, in the last few months, subject to examination for compliance which is enormously important. That rulemaking is already done.

I expect in this year rather imminently that we will also propose a rule to provide greater transparency of order routing for institutional orders as well as enhancing the existing disclosures that are made on the retail side. Again, that is very important information to our markets to ensure fairness, to see what your agents are doing as they execute your order. So those are examples.

Senator CRAPO. You referenced the telephonic meeting on July 8th. That is a report from EMSAC that you were referencing there?

Ms. WHITE. Yes. That will be a further discussion by the full committee of their subcommittee's recommendation on the maker-taker pilot. We are also taking up some other issues at that meeting.

Senator CRAPO. So following that meeting, do you expect that the Commission would be in a position to take the next action and move forward? Or when do you expect that this could get to a commission decision?

Ms. WHITE. Well, the next step is indeed for the staff of the Commission and the Commission to take in the recommendation from the committee, but it will be up to the staff and the Commission as to what to do and what the parameters should be. I do think it is important to do this in a well-designed pilot because it really does touch on a very important issue where we need the data.

Senator CRAPO. Do you have any feel for about when the Commission—

Ms. WHITE. I cannot give you a specific time, but it is a this-year priority to move that along as soon as we get the recommendation.

Senator CRAPO. All right. Thank you.

Ms. WHITE. And when I say "move it along," I mean consider it at the staff and Commission level.

Senator CRAPO. Thank you. I also want to thank you for your past efforts to improve the transparency of the Financial Stability Oversight Council process by seeking public comment on the report by the Office of Financial Research on the asset management industry. There have been several hearings on the Financial Stability Oversight Council that focused on ways to improve transparency, accountability, and communications.

In the Subcommittee hearing that Senator Warner and I held last year, the witnesses agreed that FSOC needed to provide ac-

tionable guidance to designated systemically important financial institutions on how they could derisk and ultimately shed their designation label, what has been referred to as an “off ramp.”

Do you agree that it would be appropriate to take additional steps to increase transparency, accountability, and communications in the FSOC process?

Ms. WHITE. I think that is something that we have to be committed to doing as we go forward. That is not something that may be completed at any point in time, and I do think FSOC is committed to looking for ways to enhance the transparency of its process. The so-called off-ramp process is an existing process under the FSOC rules and guidance. It is an annual process. But I also take your point about greater transparency regarding what the factors are that may be involved in that.

Senator CRAPO. Thank you.

Chairman SHELBY. Senator Merkley.

Senator MERKLEY. Thank you, Mr. Chairman.

One of the most egregious things in the lead-up to the meltdown were firms that put together securities and then they sold them, saying, “These are the best things since sliced bread,” but while they were privately taking bets so securities would fail because of the details that they knew about the securities they had packaged. Carl Levin championed an end to this type of egregious conflict of interest at Section 621. Here we are now 6 years later, and we do not even have a draft rule. Why not?

Ms. WHITE. I agree it is an enormously important rule, and I obviously know well the range of transactions that you are talking about that it was intended to address.

As I know you know, Senator Merkley, there was a proposal issued in September of 2011, which is still outstanding, where we got tremendous comments. This was actually before the SEC had adopted its economic guidance. So, for some of the comments that we got, one was that we must really do very intense, good economic analysis. We also got comments that it was not tough enough, or it was too tough or it swept in too much or did not sweep in enough.

It has proved to be much more complicated than certainly our experts in the agency envisioned. I think we asked in that proposal 100 questions, and that is a very large number—for example, who is covered, what is covered, and all sorts of various interpretation issues, including with respect to what the exceptions should be.

We had a recent comment come up as late as December 2015 as to whether certain Fannie-Freddie guarantees would be covered because of the concern that those securitizations could not continue, at least under the parameters of the proposal. So it is one where the staff is working very hard to get a reproposal done as soon as it can, but it has proven to be very, very difficult to draw the right lines.

Senator MERKLEY. This is one of the most direct examples of unacceptable Wall Street behavior where Congress took a very clear stand. Wall Street desperately wants this to never happen. The SEC has gone year after year after year failing to get it done under the argument it is just too complex, it is just too difficult. I do not think anybody in America buys that this type of conflict of interest

is too difficult. The instructions have gone to the SEC. The SEC has failed the public on this issue and allowed this type of conflict of interest practice to continue, and I think it is absolutely unacceptable. And I would have said the same to your former Chair back in 2013, but here we are 3 years later, and now the responsibility rests with you.

Let me turn now to the issue of political spending being disclosed by corporations. A million public comments have been received supporting disclosure because the owners of the company, the stockholders, feel like if the company is spending their money on political activity, they have a right to know. And under the concept of money is speech, if you do not get to know how your own money is being spent, it is really stolen speech. And that is bad enough, but it is certainly material to what investors understand about the future prospects for that company. What are they advocating for? What are they lobbying for? Who are they lobbying for? Who has which philosophies or which positions?

And so both from the viewpoint of individuals getting to know how their own money is being spent on political speech and from the view of a material issue related to the future performance of the company, it is imperative that there be disclosure.

There was such a plan on the agenda when you took the chairmanship, but in October of 2013, you took it off the agenda. Not even to hold the conversations, to prepare the way on this, this is an issue of freedom of speech. It is an issue of knowing how your own money is being spent. It is an issue material to the future of the company, and you took it off the agenda. Why would you do such a thing?

Ms. WHITE. Well, let me say first that I do deeply respect and understand the very deep interest in this issue on all sides, and I think it is also important to note that if the spending is material in the context of a particular company as we sit here today, that would need to be disclosed under the Federal securities laws. And we also have through our shareholder proposal rule, Rule 14a-8, avenues for shareholders to raise this issue with their particular companies, and they make great use of that avenue. The average approval rate for such proposals last year was about 26 percent. In some companies over the years using that avenue, there have been a few majority votes by those shareholders, and those companies have generally gone ahead and made those disclosures voluntarily. Certainly in large companies the number of them that voluntarily disclose political contributions has grown. I think more than half of the S&P 500 now provides that disclosure voluntarily, which I think is a good thing.

In terms of the Reg Flex issue, which is what I think you are raising, I think there is some misunderstanding about what was on the SEC agenda and perhaps even, what I did in reviewing the Reg Flex Agenda as I found it. What has not been on the Reg Flex Agenda at the SEC before I arrived or after I arrived is to go forward with such a rule. What was on the Reg Flex Agenda, put on there in late 2012 and was there when I arrived, was an item reflecting that the Division of Corporation Finance would research and consider whether to recommend a rule proposal on this subject. My predecessor wrote to Congress in March 23 in response to a

congressional investigation on this issue that neither she nor the Commission nor the staff had reached any conclusion about that—whether to recommend a proposed rule—and that no one was actually working on a rule proposal at that time.

Shortly after I arrived, the first Reg Flex Agenda was due, and so I basically carried forward for the most part what was on the previous agenda, including that item. In the fall, when I had been there a little longer, I had a chance for the staff to do a deep dive of all the items on the Reg Flex Agenda, many that had been there, by the way, for many years and were aspirational. And the Reg Flex Agenda instruction requires you to put on that agenda the items that you reasonably believe you can complete in the next 12 months.

And so as you know, I have prioritized since I arrived here completing the congressional mandates under the Dodd-Frank Act and the JOBS Act as well as, as we went forward, certain mission-critical initiatives like equity market—

Senator MERKLEY. I am way over my time, and so in courtesy to my colleagues, I will just stop you there because we cannot get a full history. But it was listed at the proposed rule stage in April 2013 and was taken off in 2013. You have the sole power on the Commission to establish the agenda. This is an issue that goes to the core of who we are as a country that people cannot spend your money on political speech without telling you how the hell they are spending it or that you as an owner have a full right to know how your funds are being spent. I think for you to unilaterally remove it from the rulemaking agenda was an egregious affront to these core issues of our Republic. It came after pressure, political pressure. I think it is unacceptable. I think you should put it back on the agenda.

Ms. WHITE. That item and about 20 other items that were on the previous agenda were removed for the reasons that I said, and it was never on there to advance a proposed rule.

Chairman SHELBY. Senator Rounds.

Senator ROUNDS. Thank you, Mr. Chairman.

Good morning, Chair White. You have stated in the past that you believe there should be uniformity between the fiduciary rules issued by the Department of Labor and the SEC. The Committee on Homeland Security and Governmental Affairs recently released a staff report regarding the DOL's fiduciary rule. The report found, among other things, that there was extensive disagreement between staff at the SEC and the DOL over the fiduciary rule.

The report found that, in addition to the DOL refusing to conduct a quantitative analysis of the costs and benefits of alternative approaches to the rule, as recommended by the SEC and required by the Executive order, the staff economists from both agencies also had disagreements over the rule. In fact, the report found that the disagreements reached the point of the Labor Department staff writing, and I quote, "We have now gone far beyond the point where your input was helpful for me. If you have nothing new to bring up, please stop emailing me about this topic."

Chair White, how do you believe the SEC can structure a uniform fiduciary rule when it appears there are inherent disagree-

ments between the two agencies over the fundamental goals of the rule?

Ms. WHITE. I think what I have said in the past is I believe that there should be a uniform fiduciary duty rule for broker-dealers and investment advisers when they are giving securities advice to at least retail investors. That is really under our rules. The Department of Labor and the SEC are separate agencies, and so our rules are not identical, including before the DOL rule was adopted in certain areas where our registrants may overlap with theirs.

In terms of the Department of Labor/SEC staff interactions on their rule proposal, I think the comment you mentioned is from 2012, actually, on the prior proposal, so I was not here then. But I will say that the SEC staff did give substantial technical assistance to the DOL staff on the current, now final but then proposed, rule, including technical assistance on our own rules and what they provided, but also the possible, impacts on the availability of reasonably priced advice by brokers and what the impact would be on the broker model itself.

The nature of those exercises—and we have done it with other agencies, too, on other rules where we have that technical assistance to provide—was not really to reach agreement but to make sure that we were giving our best technical assistance and input to the Department of Labor, which then obviously made the decision as to what the proposal should be, and put it out for notice and comment. I think the notice and comment was focused on some of those same issues.

Senator ROUNDS. Would it be fair to say that, based upon the rule which is in effect right now coming out of DOL, would it be fair—and I do not want to put words in your mouth, but would it be fair to suggest that there would be concerns yet as to the availability of investment advice being made available to the smaller investors and perhaps a limiting of some of that advice right now based upon the traditional ways that we provide investment services to some of your smaller investors in the United States today?

Ms. WHITE. Again, I am very focused on that issue myself in connection with our work on a uniform fiduciary duty rule under Section 913. Certainly the Labor Department was focused on it, as reflected in their notice and comment period. I think certain changes were made in response to that concern and possible impact. But I think to some degree—and this would be true of our rules, too—you need to see what happens as the rules are implemented. Certainly we are available to provide whatever help and assistance we can to our registrants if they run into a conflict with our rules. Nobody has come to us yet for that, though.

Senator ROUNDS. My concern is that sometimes as we try to protect individuals, we actually limit the availability to them of opportunities to invest. And I want to go into one other area here, and that is, one of the SEC's goals is to facilitate capital formation. One recent trend along these lines is the increase in the issuance of private shares which can have significantly less disclosure requirements relative to public share offerings. Private offerings can only be sold to qualified high-net-worth investors.

In 2014, more than \$2 trillion was raised privately. Private stock issuances under the SEC's Regulation D accounted for more than

\$1.3 trillion of this amount. In comparison, registered public offerings amounted to approximately \$1.35 trillion in 2014.

Are you concerned by the fact that issuances of private stock have now outstripped public shares sold to all retail investors in terms of new issuance? I mean, doesn't this kind of point to a trend here of kind of the guys who can afford the—the guys who are capable of investing large amounts of money are basically providing a lot of the new public issuances, they are receiving it, and the smaller retail folks seem to be not in that position? Isn't there something going on here that maybe is not moving in the right direction?

Ms. WHITE. I think what we have an obligation to do—and we do is monitor both the private and the public markets very closely and continuously. As you know, we have a tripartite mission, which is to protect investors, assure the fair and efficient functioning of the markets, and to facilitate capital formation. I do not see those three pieces to be in conflict, but they certainly need to be taken into consideration in terms of everything we do.

I think the point you are also making is on who should be within the definition of “accredited investor,” which obviously drives a lot of what happens on the private side of the markets. Clearly, from, our inception, that concept is meant to protect investors who may not be able to protect themselves. That obviously hits the core of our investor protection mission, which we feel obviously very strongly about.

In terms of the public markets, one thing I do think we have responsibility for and we certainly, are looking at this constantly is whether there is something about our rules for the public markets that is unnecessarily driving away, public offerings. So we look very closely at that. Obviously, we have had with the JOBS Act the IPO on ramp, which makes it somewhat easier to do that. Again, we are still focused on investor protection, but I think that whole range of issues deserves and is getting very close attention from the SEC.

We recently published, as you may know, the staff's accredited investor study with a series of recommendations on that, and that also touched on some of the issues you are mentioning.

Senator ROUNDS. Madam Chair, thank you.

Mr. Chairman, thank you for the time.

Chairman SHELBY. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman.

Chair White, I would like to bring you to the plight of the 3.5 million United States citizens on the island of Puerto Rico. This is a situation where Puerto Rico finds itself paying 33 cents of every dollar that it has toward its debts. The Government has been forced to make excruciating decisions to shut down schools, scale back essential services. Hospitals with no access to power are closing the doors. The island is losing at least one doctor each day, and we have one of the most significant migrations out of the island to the mainland in quite some time, which underlines the critical importance of a congressional solution that will allow the Government to restructure its debts and protect the people.

But beyond those reasonable and necessary solutions that should come from the Congress, the people of Puerto Rico deserve to know

whether illegal activity by advisers to Puerto Rico and its municipal entities controlled and contributed to the current debt crisis. Dodd-Frank explicitly mandated that the SEC and the Municipal Securities Rulemaking Board protect municipal entities, and yet, despite the widely acknowledged problems on the island, neither the SEC nor the MSRB has held one hearing, Commission meeting initiative, or given any particular attention to Puerto Rico's debt crisis, at least not to my knowledge.

So what I want to know is whether municipal advisers, underwriters, and broker-dealers—all of whom are subject to the SEC and MSRB regulations—that operated in Puerto Rico have done so free of conflicts of interest, whether they packaged and sold bonds worthy of the savings of hardworking investors, and, most importantly, whether they have acted in the best interests of the Puerto Rican Government and people. How will the SEC pursue this element of their crisis?

Ms. WHITE. I could not agree more about the state of that crisis and that what our Government—collectively in my view—needs to do to address that in a positive way. But in terms of the SEC's jurisdiction there, we have actually very closely attended to investments in various funds with bonds that may be at risk in terms of investor protection. We put out guidance on some of that from our Division of Investment Management.

We also have brought two public enforcement actions that have dealt with brokers who have misled investors about the riskiness of those bonds. And while I cannot—

Senator MENENDEZ. In Puerto Rico?

Ms. WHITE. Yes. Yes, both of them—one I think in this year and one in 2014. I can give your staff the details of those. And, again, I cannot comment on specifics of anything ongoing that we are looking at now, but I think I can say that we are very focused on the issues that you raise in some of the other work we are doing.

Senator MENENDEZ. So you know, several colleagues of this Committee and others have joined me in a letter to you and to the Commission urging you to be not just the cop on the street in Wall Street but also in San Juan, and to make sure that those who may have contributed to this crisis are fully prosecuted, because at the end of the day, if that can take place there, it can take place anywhere. And sending a strong message that it is not acceptable is critical. So I look forward to your continuing work in that regard, and I would like to be advised of what is happening when it is available to be public.

Second, I would like to go back to the question of corporate political spending. I continue to believe that transparency and disclosure to shareholders is of the utmost importance, both as a matter of corporate governance and investor protection. And it is not just me; 1.2 million Americans have implored the SEC to act by virtue of their commentary during the rulemaking.

So it has been nearly 6 months since I, along with 96 Members of Congress, wrote to you asserting that the SEC retains the authority to take critical steps to prepare for a possible rule on the issue of corporate political spending. And as we indicated in the letter, we expected and continue to expect the agency to move forward with plans to prepare for a rulemaking.

Now, I know that the 2016 Omnibus Act is seen by the Commission as preventing them from taking the type of action, but that action specifically talks about issuing, implementing, or finalizing a rule. It does not speak to preparing a rule for that moment, because I can assure you that that provision will die. That provision will die. And we need not wait for it to die when 1.2 million Americans have said to you, probably an unprecedented number, that they want to see a rule in this regard.

So I hope that—and I would like to get from you a sense of whether or not—I mean, we have pending nominees to the SEC. I did not care for the way either of them answered me on this question. I would like to know, Are you going to at least prepare and respond to those 1.2 million Americans and nearly 100 Members of Congress who believe that you should move forward in this regard?

Ms. WHITE. Senator, again—and you may have heard some of my answers to Senator Merkley's questions—I deeply respect the strong views of those that you have mentioned. There are very strong views on both sides of this issue, and I have also mentioned how the disclosure is developing, both voluntarily and through our shareholder proposal process. But the issue of the SEC doing a rulemaking to mandate political disclosures by all public companies is not on our Reg Flex Agenda. So with or without the appropriations language the priorities that we are pursuing, and pursuing as hard and as fast and as well as we can, are really the ones that I have outlined since my early days here, which are the mandated congressional rulemakings and certain of the mission-critical initiatives. I have talked about asset management and equity structure.

So I think that is the status now, and I say that with a full appreciation of the deeply held views on this, on all sides, including by 2,000-plus unique comment letters that we have gotten on the petition that you reference.

Senator MENENDEZ. I will just close, Chairman: 1.2 million Americans, I think very rarely has the SEC seen that extent of commentary, tells you the incredible importance that people believe in the nature of limited corporate spending at a time in our national politics that determines decisions in every asset of our life. And so I think that should be a far greater level of consideration by the SEC than it presently is.

Thank you, Mr. Chairman.

Chairman SHELBY. Madam Chair, before I recognize our next Senator, we have over 300 million people in this country, so 1.6 million would be about a third of 1 percent and self-generated. I hope you as Chairman of the SEC or any agency would not react to generated mail from Republicans or Democrats but would do what is best for the country and also under your jurisdiction. It is my understanding that this is under the basic jurisdiction of the Federal Election Commission, for what it is worth.

Senator Toomey.

Senator TOOMEY. Thank you, Mr. Chairman.

Chair White, welcome back. You observed a few moments ago that one of the responsibilities of the SEC is to facilitate capital formation. There is legislation that I think would be very constructive to that end. It was introduced in the House by Congressman Mulvaney, and what it would do is streamline some of the regula-

tions affecting business development companies, BDCs, and included in that is a modest increase in the leverage they would be permitted to use from a 1:1 ratio to a 1:2 ratio.

If this were adopted, it seems to me, BDCs would be better able to provide loans that they do provide to small- and medium-sized companies, which, by the way, are finding it more difficult to access bank loans given the regulations of Dodd-Frank. It would also allow better returns for investors, potentially, with some added risk that would be fully disclosed to those investors. And it has demonstrated extremely broad bipartisan support in the House. I think his bill passed the House Financial Services Committee 53–4, and it was included in legislation that passed the House floor overwhelmingly.

We have not taken this up yet, but my understanding, Chair White, is that you have some concerns about the leverage component in this, and I am wondering if you could briefly, because I have got limited time, tell me why you are concerned about increasing the leverage of BDCs.

Ms. WHITE. Yes. First, let me just say that I think BDCs have been very good vehicles for growth. They were designed to be that for developing companies that might not otherwise be financed. I think the original statute was passed in 1980.

The current reality is that retail investors hold the majority of those shares, so that always raises our investor protection antennae. We have worked over the years—the staff has to try to facilitate BDCs’ operations because they have a patchwork quilt of regulations because of their exemptions from some of the Investment Company Act provisions.

I have written about this. I think when I first got here in October of 2013, there were some changes made in the bill, which I think improved it. I appreciate those. I also wrote a letter late last year to Chairman Hensarling and Ranking Member Waters. I still have investor protection concerns, or I would not have written the letter—

Senator TOOMEY. What is—

Ms. WHITE. One is leverage.

Senator TOOMEY. What is the concern about the leverage?

Ms. WHITE. One is leverage.

Senator TOOMEY. What about the leverage?

Ms. WHITE. It doubles the leverage, which means that your upside and downside potential are multiplied or are multiple, and it is a higher level of leverage than any sort of its counterpart kinds of funds have—

Senator TOOMEY. So—

Ms. WHITE. Second, I think it allows more investment in financial institutions than was originally conceived and allows investments in registered investment advisers, so—

Senator TOOMEY. Right, so let me—I have got very limited time here. So it is true that it increases the risk profile, it increases the exposure. But so does investing in a bank. A bank is a highly leveraged entity. Retail investors are allowed to buy securities on margin. Do you support allowing retail investors to continue to buy securities on margin?

Ms. WHITE. I am certainly not opposed to that, but I think there are more issues with respect to this bill and risks with respect to this bill than just that.

Senator TOOMEY. Well, but that is what—

Ms. WHITE. That is one of them.

Senator TOOMEY. —leverage is about, right?

Ms. WHITE. That is one of them.

Senator TOOMEY. OK. I thought leverage was the main concern. I would simply observe that there are many, many opportunities for an investor to take on leverage if an investor sees fit to do so. Buying options, for instance, can create the equivalent of enormous leverage, much, much more than this very limited increase that would be, after all, managed by a professionally managed company. So I would really urge you to consider that among the various ways a retail investor can achieve leverage, this would be a very modest—it is heavily regulated. It is run by professionals. And the upside benefit I think is very significant.

Let me touch on another item here. I think the SEC has a proposed rule that would govern the use of derivatives by registered investment companies, and, of course, derivatives are used for a variety of reasons to achieve fund objectives. They are all disclosed. It is articulated. If the SEC were merely consolidating previous guidance letters, then I rather doubt we would have seen the volume of comments that have resulted. In fact, I think there are some things new. One that I am concerned about is that the exposure that is used to cap the amount of derivatives is based simply on the aggregate notional amount of those derivatives when, in fact, notional amounts are a terrible proxy for risk. They do not measure risk at all. So why are we using the notional amount to determine the limit on these investment companies' derivative holdings?

Ms. WHITE. That is one among several important issues that we teed up in the rule proposal, and one, as you point out, we have gotten a lot of comments on, which the staff is very thoroughly going through as they consider what their recommendation will be for the final rule. That is probably one of the most frequently commented on aspects of it—not all comments are critical, mind you, but a number are for the reasons you state.

Senator TOOMEY. So is it your intention that there will be some modification here and that there will be a measure other than simply the really meaningless notional principal amount?

Ms. WHITE. Again, I cannot get ahead of the process, but I can say that we are very focused on that issue, and the nature of our notice and comment process is that we very seriously consider all of the comments and try to basically propose a final rule that is optimal and better than our proposals.

Senator TOOMEY. OK. Thank you, Mr. Chairman. Thank you.

Chairman SHELBY. Senator Donnelly.

Senator DONNELLY. Thank you, Mr. Chairman. Good morning. Thank you so much for being here.

In 1982, the SEC adopted Rule 10b-18 to provide a safe harbor from market manipulation liability on certain stock buybacks. Buybacks could have been considered market manipulation back then. Recently, in my home State of Indiana, 2,100 workers were

let go by a highly profitable company in order to get \$3-an-hour jobs to Mexico. The CEO said returning cash to shareholders continues to be a top priority. We are targeting \$22 billion of total shareholder returns through share repurchases and dividends through 2017. Of that \$22 billion, \$16 billion will come in the form of stock buybacks—\$16 billion in stock buybacks, while firing 2,100 workers in Indiana in order to get \$3-an-hour jobs in Mexico to help fund the stock buyback.

I will also note that the savings they get from this are less than one-half of 1 percent of the amount of the stock buyback.

So my question is: You know, in 1982, this could have been considered market manipulation. What does the SEC think of actions like this now?

Ms. WHITE. Well, the safe harbor rule that you mention does not immunize companies from liability for market manipulation if it occurs. It is basically designed to impose some rules to at least try to prevent market manipulation. For example, if the buyback is done on the basis of material nonpublic information a fraud action can be brought. The safe harbor does not deal with that at all. I am acutely aware of the whole set of issues with buybacks. They have gotten a lot of attention in a lot of situations, and so we are focused on it.

But the SEC does not—

Senator DONNELLY. Well, let me ask you this—

Ms. WHITE. —dictate how—OK.

Senator DONNELLY. Should the SEC play a larger oversight role in overseeing stock buybacks as this has been funded by firing American workers?

Ms. WHITE. I take your point completely. I do not think the SEC has the authority to tell a company how to spend its money. What we do have, though, are disclosure rules with respect to buybacks that provide transparency to investors and the public of companies that buy back at least shares registered with the SEC under Section 12(g), and we are addressing that issue in our disclosure effectiveness review and our recent SK—

Senator DONNELLY. Let me ask you this—

Ms. WHITE. —constantly to see whether we should—

Senator DONNELLY. —do you think this—

Ms. WHITE. —and make that disclosure more—

Senator DONNELLY. Do you think this was the conduct envisioned when the rule was changed back in the 1980s?

Ms. WHITE. I am not sure about the conduct that you are describing. Obviously, the way you are describing it—and I am not doubting it at all—it is a horrible set of events and had obviously very significant and unfortunate negative consequences. But, again, I think what we have designed with our rulemakings—and we are looking at it again to see if we cannot do more—is to avoid market manipulation, which is within our jurisdiction.

Senator DONNELLY. Well, in the SEC's eyes, who is the corporate responsibility to? Is it to just the shareholders? Or do they owe a duty to the entire corporate enterprise, including workers? You know, what is the corporation's responsibility in the eyes of the SEC? Who is it to?

Ms. WHITE. The fiduciary duty of the board, for example, and the officers is to their shareholders. But by my saying that, I do not want to imply that I think there are not duties and responsibilities—

Senator DONNELLY. Well, does the SEC assume that they have any responsibility to their workers, or can they just fire them willy-nilly?

Ms. WHITE. That is not a subject that is within the jurisdiction of the SEC unless it is something that has an impact on what is within our authority.

Senator DONNELLY. When you look at this, I think a big part of this is corporate short-termism, if you want to—you know, I do not know that that is a very technical term, but it is the reality of life. I met with these workers this morning. They were making \$13 an hour. Their CEO made 11. The CEO before him took over \$150 million out on his last day. And they are making 13 bucks an hour on a very, very, very profitable plant, and they are fired so their jobs could go to \$3 an hour in Mexico to help fund a stock buyback. Do you inherently see something wrong with this business model? Is the American dream that we all fight for? Is this what the SEC expects on conduct from the corporations that you regulate?

Ms. WHITE. What we expect from the corporations we regulate—and certainly as citizens expect from those we do not regulate—is fairness to not only their shareholders and the fiduciary duty they owe to shareholders, which is within our direct bailiwick, but also to their employees as well. There are studies out there on the buybacks and the benefits and the detriments that go both ways depending upon the context of the particular company when they are buying back, what they are doing with their funds, what they have to do with their funds and so forth. But I take your point.

Senator DONNELLY. Thank you, Mr. Chairman.

Senator COTTON. Thank you. Thank you, Mr. Chair.

I want to talk a little bit about FINRA and its structure. FINRA is defined as a self-regulatory organization. Is that correct?

Ms. WHITE. Yes.

Senator COTTON. Does FINRA operate with a mandate from the Federal Government?

Ms. WHITE. FINRA is, as you point out, a self-regulatory organization that is a membership organization, but it is certainly an organization that is primarily responsible for the surveillance and regulation of broker-dealers.

Senator COTTON. Does it use tools that are similar to or typical of those of an independent Government regulatory agency?

Ms. WHITE. Certainly on its exam and enforcement side. They have tools we do not have, frankly, because it is a membership organization. There are things they can do that we cannot do under our own authorities, but they certainly use surveillance tools, they use enforcement, and they use exams, which are similar.

Senator COTTON. And they make rules that will govern the conduct of their members?

Ms. WHITE. They certainly make rules. Many of them are subject to SEC approval, but yes.

Senator COTTON. Are there any other private organizations that are similarly structured and oriented within the securities law space?

Ms. WHITE. Not at the present time.

Senator COTTON. What sort of input, to your knowledge, do FINRA members have into FINRA's regulatory policy agenda?

Ms. WHITE. I do not know the specifics of that. Obviously, they have a board structure, and they are a membership organization.

Senator COTTON. What authority does the SEC have over the FINRA Board?

Ms. WHITE. We certainly oversee FINRA. We inspect FINRA, our exam staff does, on various issues, and some of their programs. We have some authority over their rules as well. Some of their rules.

Senator COTTON. Do you have the power to appoint board members?

Ms. WHITE. No.

Senator COTTON. To remove board members?

Ms. WHITE. No.

Senator COTTON. So FINRA exercises investigative and prosecutorial functions related to SEC rules, Federal securities laws, and its own rules?

Ms. WHITE. Yes. Generally speaking, yes. There are some exceptions to that, but yes.

Senator COTTON. Are those functions executive power, in your opinion?

Ms. WHITE. They are not. I know this is an issue that people talk about all the time, but they are not a Government entity. But the answers I gave are accurate, I believe, in terms of their powers.

Senator COTTON. To your knowledge, does FINRA employ paid lobbyists?

Ms. WHITE. I do not know.

Senator COTTON. OK. Thank you.

I would like to turn to a separate topic—"shareholder activism," as it is sometimes called. On a number of occasions, you have commented on the role that economically motivated investors play in the capital markets. In a speech last year in New Orleans, you noted that, "An intense debate is taking place in the business, legal, and academic communities as to whether activism by hedge funds and others is a positive or negative force for U.S. companies and the economy." In that speech you also said that the SEC's role in any given contest between shareholders and boards of public companies "is not to determine whether activist campaigns are beneficial or detrimental but, rather, to ensure that shareholders are provided with the information they need and that all play by the rules."

So putting aside the question of any particular dispute, any particular company, any particular investor, do you believe that, on balance, engaged shareholders provide critical market-drive checks and balances to provide greater corporate productivity and management accountability?

Ms. WHITE. That is a very broad question. I certainly think they can.

Senator COTTON. OK. You have also spoken favorably in the past about the role of cost/benefit analysis at the Commission. Given

your views on the importance of a data-driven approach to developing public policy, are you concerned about some appeals to emotion that we see from some involved in the debate about so-called activist investing, which is sometimes also portrayed as short-term investing?

Ms. WHITE. The SEC is an independent agency and has always been. I am an independent head of that agency, and so I think it is very important for us to keep our eye on the ball and make decisions based on the merits, which I think we do.

Senator COTTON. So in this space, you are committed to developing rigorous econometric data on the marketplace impact of potential disclosure rules changes or any other limitations on marketplace participants where rules changes would be proposed and adopted?

Ms. WHITE. Certainly any of our rules are subject to that economic analysis.

Senator COTTON. OK. Thank you for that. Thank you for your appearance today.

Chairman SHELBY. Senator Tester.

Senator TESTER. Thank you, Mr. Chairman. And thank you for being here, Mary Jo. I appreciate the work that you do.

I want to talk a little bit—because I appreciate you taking the blame for a lot of stuff, but I want to talk to you about the Commission right now. How many members are active on your Commission? How many members do you have on the Commission?

Ms. WHITE. We have three.

Senator TESTER. OK. And it is my understanding—and correct me if I am wrong—it has been that way for about the last 8 months, right?

Ms. WHITE. Do you want me to give you the hours and the minutes? The last 6 months.

Senator TESTER. Six months. And is it true that since you have only got three, any one of those three can say if they do not like a potential vote that might be coming up, just stay away, and then you do not have a quorum and you cannot work?

Ms. WHITE. Well, as a Commission of three, we have to have all three Commissioners to do a rulemaking.

Senator TESTER. Yes, so any one of them can walk away from the table and you are sunk, right? That is pretty good power.

Ms. WHITE. They could, but I think we are very focused, all three of us, on getting the work done, too.

Senator TESTER. Well, that is good. What about your staffing? How are you staffed up? Do you have adequate staff?

Ms. WHITE. I think the SEC is a significantly underresourced agency for our responsibilities.

Senator TESTER. Would that change if you became a self-funded agency?

Ms. WHITE. It would.

Senator TESTER. Could you give me sort of—I mean, have you run any—are you 20 percent down, 30 percent down on staffing measures?

Ms. WHITE. I have certainly talked mainly in the context of our ability to cover on the examination side investment advisers, which are obviously enormously important to investors, particularly retail

investors. I have also talked about how we are so outspent on the IT side by those we regulate that in those areas we have done some analyses. But, again, I respect the appropriations process, the congressional oversight process, and try to make the best case I can for more and adequate resources.

Senator TESTER. Well, I think that—and, look, I mean, there has been ten people speak ahead of me, and some of them have been very critical. Some on my side of the aisle have been very critical about you not doing some of the work that is assigned. And I can be critical, too. And, by the way, I am. But the fact is that you have got to play the hand that is dealt to you, and the hand that is dealt to you is a pretty weak hand right now, in my opinion. Would you agree that if you were fully staffed up and you had five Commissioners you would be much more effective and would get more work done?

Ms. WHITE. I think the answer to that is yes. Certainly being staffed up would accomplish that.

Senator TESTER. So we had a fiduciary rule that several have talked about, Senator Rounds and others, that got put out by the DOL, and I was critical because I thought this was a job you should have done, and I think if you had been fully up, you would have got it done. But, unfortunately, it did not happen. Are there any plans to get that fiduciary rule happening from the SEC's standpoint?

Ms. WHITE. I am certainly committed to getting it done because I think it is of enormous importance. But I have also made clear how difficult and long a road that is under Section 913 of the Dodd-Frank Act and that I am one vote.

Senator TESTER. Yes, and so fair point. And it has been documented there were some differences between the SEC and the DOL when that rule was put out. And I do not hear you saying it is going to be done before this Administration is out the door.

Ms. WHITE. Well, I am committed to moving it as fast and as well as I can, but I cannot give you that commitment now.

Senator TESTER. In all practicality—

Ms. WHITE. It is a longer route than that.

Senator TESTER. OK. So we have got the DOL rule. So the question occurred to me: Do you have to enforce the DOL rule?

Ms. WHITE. We do not.

Senator TESTER. So who enforces it on investment advisers and broker-dealers?

Ms. WHITE. Enforcing their rules is their responsibility.

Senator TESTER. So the DOL will enforce the rules on investment advisers and broker-dealers.

Ms. WHITE. They would enforce their own rules with respect to whoever is subject to them.

Senator TESTER. Traditionally, wasn't that a job for the SEC?

Ms. WHITE. Not as to their rules, no.

Senator TESTER. No, but as far as investment advisers and broker-dealers go?

Ms. WHITE. And still is. Except not with respect to their rules, but with respect to our rules.

Senator TESTER. So tell me how this is going to work. I mean, practically, how is it going to work?

Ms. WHITE. Well, I think it is independent agencies, independent rules. We have had before this rule rules by DOL and rules by the SEC that overlap, so to speak, and we have managed our way through that pretty well. We clearly will watch this as it goes forward. And if issues arise we will certainly be available, and I am sure DOL will be available, to coordinate if a conflict should develop.

Senator TESTER. OK.

Ms. WHITE. And if and when—I hope we go forward with our own rulemaking—obviously, we will coordinate with them about any new issues that might arise with respect to that.

Senator TESTER. I appreciate it.

Mr. Chairman, I will put a few more questions in the record, but thank you very much.

Ms. WHITE. Thank you.

Chairman SHELBY. Senator Moran.

Senator MORAN. Mr. Chairman, thank you. Chairwoman, thank you very much for your presence today. We have had a conversation in the appropriations process I want to continue to ask you about. It deals with the regulation of the National Marketing System. The question I have is whether the NMS plan governance model should be reformed to reflect evolution of our markets and add additional participants as voting members. My question is: Does the SEC currently have legal authority to approve the addition of additional market experts as voting participants in the governance of NMS plans?

Ms. WHITE. Subject to our overall SRO rule process, we could do that. One thing I should mention is we actually have recommendations coming from the subcommittee of the Equity Market Structure Advisory Committee on this very subject, but we are typically in the position of approving a rule filing. But we can also issue orders to solicit rule filings, if I could say it that way.

Senator MORAN. So maybe there is more to this story than me just asking you whether you have the authority. Is there something in the works? Can you bring me up to speed on this topic?

Ms. WHITE. It is certainly a topic that the Commission is focused on, the staff is focused on, and so is our Equity Market Structure Advisory Committee, and, in particular, I think it is called our Trading Venues Subcommittee. And that is one of the topics, indeed, that they discussed at their last meeting with the full committee, I think at the end of April, and is or may be the subject of recommendations.

Senator MORAN. Do you have attorney personal thoughts on this topic? Or are you just waiting for those recommendations?

Ms. WHITE. I am very well aware of the issues, and I know some accommodations have been made, which other advisory participants, have not found sufficient or satisfactory. And so it is an issue I am focused on. It is an issue I continue to consider whether and what changes, if so, should be made.

Senator MORAN. OK. I want to follow up a bit on the Senator from Arkansas' conversation about FINRA oversight. I noticed that FINRA appointed a new CEO yesterday who is a former employee of the SEC. I guess my question is: How do you satisfy the need for congressional oversight of FINRA? Is it just a matter of we have

oversight over the SEC and the SEC has oversight over FINRA? Or is there a greater opportunity—we have no appropriations process there, no confirmation process. Occasionally, FINRA representation is before Congress in a setting like this, but beyond that, it seems to me that FINRA's role is growing more engaged in regulatory activities and Congress has little oversight in that regard.

Ms. WHITE. You certainly, as you indicate, have oversight authority over the SEC, who has oversight authority and exam authority over FINRA, and it is an important one, I think. And, clearly, FINRA is a very important component of our investor protection and market safeguarding.

Since I have come to the SEC as Chair, we have enhanced our oversight of FINRA and continue to do so. I think I heard Rick Ketchum, the outgoing president and CEO, indicate that he understands the interest by Congress, given their activities and the importance of their activities, in learning about them. I do not know if “oversight” is quite the right word for the reasons that you indicate. And, by the way, I think Rick Ketchum and Robert Cook, who is his successor, are just tremendous public servants, and we work very well with them. Obviously, we oversee them, but I have found them both to be extraordinarily knowledgeable—I know Rick better than I know Robert, but I know them both—about the markets, very committed to investment protection. So I think that is always a safeguard.

Senator MORAN. I think you are telling me that my assurance is that you are watching over FINRA, and we need to watch—I know you would not say this, but we need to watch over the SEC. Maybe you would say that.

[Laughter.]

Ms. WHITE. It will happen anyway, right? I think that that is correct. I guess the other part of my answer was that I am aware of the need, and we have moved in that direction to enhance our oversight of FINRA at the SEC.

Senator MORAN. You may use your position to encourage FINRA to be cooperative with Congress, open and available to us. That would be useful.

Ms. WHITE. Yes. I agree.

Senator MORAN. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman.

Thank you for being here, Chair White. As you know, the SEC's mission is to protect investors and our capital markets, and requiring companies to disclose information is a critical part of that mission. Publicly traded companies may not like disclosing potentially embarrassing or damaging information, but the SEC's job is to look out for investors, not for big companies.

Now, there is a lot you could be doing to protect investors. There are still 20 mandatory Dodd-Frank rules from 2010 that the SEC has not completed, and there are more than a million people, including countless investors and former SEC commissioners, pushing the agency to require publicly traded companies to disclose their political contributions. But instead of moving forward on issues intended to help investors, you have actually headed in the opposite direction.

Since your first year in office, you have dedicated significant SEC time and resources to a project you invented and called the Disclosure Effectiveness Initiative. According to the 2013 speech you gave, your big idea behind this project is that the SEC might be requiring companies to disclose too much information, causing investors to suffer from something you call information overload.

Now, I am all for eliminating redundant disclosures or improving the ways that information is presented but, honestly, I have never heard of the concept of information overload in the context of investing in stocks. I have never heard of the idea that investors actually want less information than they are getting.

So I have a pretty simple question. The SEC is an investor protection agency, so when you launched your project, what evidence did you have that information overload was a real problem that investors wanted you to solve?

Ms. WHITE. It is an issue, Senator Warren, that the Commission has been looking at for, really, decades, among others. But the purpose of disclosure effectiveness—and by the way, it was not invented by me—it was basically in response to a congressional mandate to do a report that reviewed our entire Regulation S-K concept.

Senator WARREN. I am sorry; when was this report that you are talking about?

Ms. WHITE. It was, filed with Congress at the end of 2013.

Senator WARREN. So are you—now, wait. Are you talking about the JOBS Act report?

Ms. WHITE. Yes.

Senator WARREN. Because that one, I actually looked at that.

Ms. WHITE. Yes.

Senator WARREN. And what was asked of you was that the SEC review one subset of disclosures to see if that subset should be modified as they apply to one subset of companies, so-called emerging growth companies. Your project has gone way—

Ms. WHITE. Right.

Senator WARREN. —beyond the boundaries identified in that law.

Ms. WHITE. Emerging growth companies are a very broad swath, as you know, of the markets.

Senator WARREN. I understand, but that is not what your project is.

Ms. WHITE. But my point is we have been, for decades at the SEC, undergoing disclosure effectiveness review. And I absolutely agree that there is nothing more—

Senator WARREN. That is not my question.

Ms. WHITE. —there is nothing more important—

Senator WARREN. My question is—

Ms. WHITE. —there is nothing more important than our disclosure powers.

Senator WARREN. —when you launched your initiative called the Information Overload, this is what you identified. And I just want to know what evidence you have that this is a real problem, that investors have come to you and said: We are worried about getting too much information. Just what evidence did you—

Ms. WHITE. First of all, the review is not limited to duplicative or overloaded information. It is really——

Senator WARREN. You mean the review in the 2012 JOBS Act?

Ms. WHITE. No, no, our review. It is meant to make disclosure more meaningful to investors. And we have also gotten comments, recently, from all kinds of constituents, including our Investor Advisory Committee, about identifying, and really not objecting to removing, things that are repetitive, duplicative, or not useful. And the purpose of this review is to make disclosure more meaningful for investors.

Senator WARREN. I did not—I started this by saying I do not have a problem with getting rid of duplication. I do not have a problem with making it more effective. The question I asked you about is whether or not this so-called information overload is a real problem identified by investors that have come to you.

Let us be honest about this. I cannot find, and you have not produced, a single investor who as complained to the SEC about receiving too much information. Investors do not want less information about the companies where they put their money. In fact, I think that is ridiculous. The SEC's own Investor Advisory Committee, which includes everyone from hedge funds to pension funds to retail investors, say recently that the current amount of disclosure—and here was their word—is appropriate.

So who wants less information to be disclosed? It is pretty clear. The National Chamber of Commerce, which represents the giant companies that have to do the disclosing. The Chamber has produced a fact-free report, whining about this nonexistent information overload problem, in 2014, shortly after you launched your initiative.

You know, information overload is a problem that was invented to justify a project aimed at making life easier for big companies and harder for investors. In fact, Keith Higgins, the SEC's head of the Corporation Finance Division and the lead on this project, kind of let the cat out of the bag in 2014 when he said in a speech the aim of this project was "to reduce the burden on companies, consistent with our mission of investor protection, wherever we can."

Now, I recognize that Congressional Republicans slipped language into the must-pass highway bill at the end of last year that asks the SEC to review disclosures with an eye toward eliminating ones that are unnecessary. Of course, that does not justify the SEC dedicating resources to this project for 2 years before that. But nevertheless, given the views of your own Investor Advisory Committee that the current disclosures are appropriate, do you agree that the supposed information overload problem does not exist?

Ms. WHITE. Well, if you go back to even Thurgood Marshall years ago, in defining materiality under the Federal Securities laws, the concern was expressed that too much information could cloud and crowd out the meaningful. I think you are describing our disclosure effectiveness review in a way that is much narrower than its intent.

Senator WARREN. That is the extent of your evidence?

Ms. WHITE. And I think one of the most important things about the disclosure effectiveness review is that we are listening to everyone. We are also talking about adding information in this review

that is needed to be added, for example on foreign taxes and other things. But it is also the manner in which the information is being provided to investors that is a huge priority of this review.

Senator WARREN. We are over our time so let me just stop you there. I have said now three times, I think, in just this brief exchange, I am fine with cutting out duplication; I am fine with making the information clearer, and as should be clear; I am fine with providing more information. What I am trying to identify is something that you specifically have targeted and talked about.

I am frustrated that, at your direction, the SEC has voluntarily spent 2 years trying to address a problem that you have no evidence exists. Instead of making up work to help giant corporations, the SEC should do its job, starting with the 20 required rules under Dodd-Frank that still are not fixed 6 years after the law was passed. Your job is to look out for investors, but you have put the interests of the Chamber of Commerce and their big business members at the top of your priority list.

Chairman SHELBY. Your time is up.

Senator WARREN. A year ago I called your leadership at the SEC “extremely disappointing.” Today I am more disappointed than ever.

Thank you, Mr. Chairman.

Ms. WHITE. And I am disappointed in your disappointment and could not disagree more with your characterization of what we are trying to do to improve our disclosure regime for investors to make it better. And we—

Senator WARREN. When you bring me evidence of this so-called information overload that you have initiated, then we can have more conversation about how disappointing this leadership has been.

Ms. WHITE. I would suggest you read the Regulation S-K concept release for the range of issues we are addressing, including that.

Senator WARREN. I would like to see some evidence that there really is a problem here.

Chairman SHELBY. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman.

Chair White, it is good to see you again. I want to move to another area of concern that I have. I have seen evidence recently—I am sure you probably have as well. RBC put together a chart of—its complexity is a little overwhelming—that there were 839 different fee structures—I am getting to the maker-taker issue—with 2,700 different iterations in terms of incentives and rebates within our market structure right now, that quite honestly give the impression that the system is rigged to direct trading through to those firms and entities that are going to give you the biggest rebate or fee structure.

It seems to me that there is an extraordinary amount of conflict of interest here in the whole question of brokers and their clients. When we look at this—and we have got, obviously, the complexity of our markets and trying to make sure—I agree with Senator Warren that we have got to get information out in a clear and transparent way. But, boy, you talk about an area that is opaque. You know, how are we going to get through this?

Now, you have talked about this back in 2014, the negative outcomes of some of these—this structure. You know, I strongly believe we need to move quickly on the maker-taker pilot. I would encourage you that when we take a look at this maker-taker pilot, that we have all venues included, both those lit and unlit.

When we think about—again, if you look at that RBC chart and then you add the dark pools behind it, enormous challenges, and that we do not—you know, I know that the Trade Act component issue added a whole series of complexity to the tick size project. And my hope is that we will not see those same kind of great to have but potentially items that dramatically slow down the ability for us to bring more transparency to our markets, and particularly in terms of this area where there appears to be an enormous amount of conflict of interest. So could you speak to that?

Ms. WHITE. First I will say—and I think I said it at the Committee meeting as well—I do think we should promptly proceed with a well-designed pilot. The discussion, of the—

Senator WARNER. How promptly do you think—I mean, considering we saw the tick size and—

Ms. WHITE. Right.

Senator WARNER. —we have gone through this a number of times and I know it has been delayed again.

Ms. WHITE. For the tick size pilot, as you know, we ended up having to order the SRO's to submit a plan that would work. And I think it is enormously important. It will launch in October of this year, but obviously it took a while to do that.

I do think you have got to be careful that you are getting the information that you need to have from these pilots. I think you may not, Senator Warner, have been in the room when I mentioned before that we are expecting a recommendation at a July 8th telephonic meeting from the subcommittee that is in charge of this subject matter at the subcommittee level to the full committee on July 8th. And frankly, I urged that to happen sooner than their next scheduled meeting so that we could move this along.

It obviously is up to the Commission, and the staff to recommend to the Commission what those parameters should be. But it is one that I think is more complicated than it seems. I do not think the system is rigged, but I think it has developed in a way that we have really got to figure out how to deal with. And I am particularly concerned about the conflicts of interest inherent in it.

Senator WARNER. Once again—

Ms. WHITE. Yes.

Senator WARNER. —you sort through this bespoke Byzantine process, and how any investor, small or large for that matter, really knows where their trades are being directed based upon the level of fees and rebates. You know, we need more market confidence, and I really think moving aggressively on this—

Ms. WHITE. I think our transparency proposals are an important part of that too, but—

Senator WARNER. Right.

Let me, the last few seconds here, go back. Senator Moran raised some of the question around market governance. And as more and more of these large exchanges do these—the SIPs, the securities exchange processors, and are making decisions to make huge cap-

ital investments in technology, sometimes that technology which may give them that fractional second advantage over others. And as I have said before, you know, I do not want to appear as a Luddite, but I do believe at some point speed and the god of liquidity being the answer is not always the completely correct answer.

But as we sort through this, and with all the various exchanges, you know, can you expand on what you said to Senator Moran in terms of governance? How do we make sure that, in terms of market governance, we have got all the right parties at the table sorting through these—sorting through these issues?

Ms. WHITE. I am not sure we are talking about the NMS governance, which we were addressing, but frankly my whole idea for the Equity Market Structure Advisory Committee was to try to bring in expertises across the range of constituents, and also to make sure we had a panel at every one of those meetings that had everybody else there that had a different point of view and an expertise. And I have been very pleased with it so far. It is also something that focuses and I think moves along more promptly the Commission's comprehensive review of these market structure issues, and it really needs to be there.

In terms of the speed issue, certainly you can get to diminishing returns. I think you had that conversation with Steve Luparello at your subcommittee hearing. I do not think you roll back technology. We have had tremendous benefits, obviously to retail investors and institutional investors in our markets from the technological advances.

Sometimes people talk about high-frequency traders as if they are one thing, and they are not. They are not monolithic. They have different strategies. And so, one of the proposals that the staff is working on is an antitrading disruption rule, which deals with, when markets are particularly vulnerable, liquidity being taken away by virtue of speed, to avoid that. So the issues, again, are complicated, but I am largely agreeing with you.

Senator WARNER. And my time expired.

I just want to say, Mr. Chairman, that, you know, as we look at complexities in the equities market, as we have seen complexities in the bond market, you know, even in the Treasuries markets, obviously the options markets—and my fear sometimes that some of these bespoke products and the incentive systems—you know, I worry that the complexity has gotten so great and the effect it has on the overall market ecosystem, that it is bleeding from one market into another.

And I appreciate, Chair White, your comments, but would love to come back and revisit with that.

Chairman SHELBY. Thank you.

Senator Schumer.

Senator SCHUMER. Thank you, Mr. Chairman.

Welcome back, Chairman White, my fellow New Yorker. And as you know, I have a great deal of respect for you, but I am going to go back to the issue I care so much about.

I just want to—the money—I am now involved in a lot of our races, our campaigns. The money that is pouring in is unprecedented and it is undisclosed. And it is a few organizations. One is the Koch brother organization, one is the Karl Rove organization,

one is the Chamber of Commerce itself—pouring in, poisoning our politics, and we do not know where that money comes from. The shareholders do not know where that money comes from.

I will have to tell you, it is more important than anything else to me before the SEC. All the things between shareholder and corporate governance pale before what is happening in America. And you want to know why people are so discontent? In part, it is because a few powerful people can send cascades of money into our system. The ads they put on TV have nothing to do with the issues they care about.

And you, frankly, are aiding and abetting at the SEC because we cannot do everything. And we know that our House Republicans—Mitch McConnell is insisting that this stay. They gain from this. And it is short-term gain because, in part, people become so discontent with the powers that be that they not only go against the—all establishment, they go against the Republican establishment. Witness the last election, the last primary.

And I just do not get it. I just do not get why corporations that give money should not tell their shareholders. These are major decisions. They have effects on the corporations. If Exxon—and I am just picking one. I have no idea what they do undisclosed, but if they put a ton of money of undisclosed into the Chamber of Commerce to fight global warming—let us just assume that—their shareholders have a right to know they may be making a bad decision.

I think you are hurting America. You are hurting America. And I know you can stay in your narrow little box and say, well, the rules of the SEC are limited, and this and that. First, a lot of people do not agree with that—most people. Second, the public. I mean, I know Senator Shelby said 1.2 million petitions is a small amount compared to the population of America. That is true, but how many other issues have you gotten 1.2 million petitioners calling you? And I wish you would change your mind. I am just so disappointed, so disappointed, because every one of our commissioners should be a citizen. They have to do things within the law. This is within the law and you have made the decision not to go forward.

So let me just ask you this. This is a relevant question. Senator Menendez touched on this issue, but I want to come back to it. John Coates analyzed that the SEC, by this—we were—the Republican leadership insisted that this provision be put in the bill. It shows you—the provision that says—you know, that says that Congress cannot touch what you do. But it was not that explicit. And as I understand it, it only explicitly prohibited the SEC from finalizing, issuing, or implementing such a rule during this appropriated period.

So do you disagree with Coates' analysis? And second, if you do not disagree with his interpretation, will you add this issue to the SEC's agenda?

Ms. WHITE. I have not studied his interpretation of it. Let me just say that I respect you enormously, and your views—

Senator SCHUMER. It is a mutual respect we have.

Ms. WHITE. —enormously. And I also deeply respect the views on all sides of this issue. I explained earlier what the SEC was

looking at when I came in, and so forth. I will not repeat that or what I have prioritized for the benefit of investors and our markets since I have been there, although I certainly made a commitment to advance the mandated rulemakings and other mission-critical issues.

But having said that, I have also talked about the avenues for shareholders to bring this issue to their companies, which is in our rules, the Rule 14a-8 shareholder proposal route. The average approval rate for those petitions last year was about 26 percent. I also certainly applaud those companies that are voluntarily providing the information, which they, by the way, are doing in greater numbers, like——

Senator SCHUMER. What else can you do to encourage companies to do it voluntarily? I understand the worst ones are not going to do it. The big violators are not going to do it.

Ms. WHITE. There is a report that came out in October of 2015 basically showing that over half of the S&P 500 now makes disclosures of their political spending. And I think 80-plus percent have policies and procedures governing their spending. So that information is certainly voluntarily being provided. Obviously our rules could never reach the Koch brothers because it is not a public company at all.

Senator SCHUMER. That is good.

Ms. WHITE. So it is not as if the SEC our rules—is the solution to campaign finance reform. I understand you are not suggesting they are, and I take your point. But essentially, the subject of doing a rulemaking has actually not been on the SEC's agenda before me or after me.

Senator SCHUMER. No, but what I am asking you is——

Ms. WHITE. Yes.

Senator SCHUMER. ——since you are not prohibited from starting the process, would you be willing to start the process?

Ms. WHITE. Well, again, the subject is not on our Reg Flex Agenda now.

Senator SCHUMER. I know.

Ms. WHITE. It is not one of the priorities that we are advancing. So do I get to that before I get to what could we do or what could not we do under the appropriations language? Obviously the appropriations language is there with its prohibitions.

Our Corporation Finance staff did look at this, actually before the item was put on the Reg Flex Agenda in late 2012, just to research and consider whether to recommend a proposed rule, not to advance a proposed rule. And they did a lot——

Senator SCHUMER. I just——

Ms. WHITE. ——a lot of work on that.

Senator SCHUMER. My time is expired——

Ms. WHITE. OK.

Senator SCHUMER. ——but I am explicitly asking you a question, which is, are you willing to start the process? That is still allowed by—even with the legislation that we passed.

Ms. WHITE. I have not researched the legal issue, but the answer is that it is not a subject that is on our current Reg Flex Agenda——

Senator SCHUMER. OK. I would——

Ms. WHITE. —because of my priorities and the priorities of the Commission.

Senator SCHUMER. I know my colleague is here. I would just say to you, your priorities are out of line with what corporate America needs and America needs. And I hope when you go to bed late at night you will think about that, because our country is basically being steered in an awful direction by a narrow few wealthy people. At the very least there ought to be disclosure.

Chairman SHELBY. Senator Heitkamp.

Senator HEITKAMP. Thank you, Mr. Chairman.

And thank you, Chair White, for appearing. As you know, I have been working on a number of provisions within the Homeland Security and Governmental Affairs Committee regarding supervision of independent agency rulemaking, obviously still concerned that we have been unable to effectuate the implementation of a long-standing executive order in legislation and have met, as you know, with great resistance from all the independent agencies.

That is not going to be the basis of my question, but I wanted just to remind you that when we met, you offered to sit down and actually have a conversation about this, because I think there is a growing amount of concern in the regulated community that there is not the kinds of safeguards that other rulemaking have. And so I want to just remind you that I have not forgotten about that.

But I want to ask you about SEC rulemaking and small business. As you know, Senator Heller and I introduced a bipartisan bill that would create an Office of Small Business within the—a small business advocate within the SEC. I am wondering if you have had a chance to review that legislation and if you have an opinion.

Ms. WHITE. Well, first let me say that I think we have really prioritized the interests of, perspectives, if I can say that, and special needs of small businesses since pretty much the day I arrived at the Commission, and we have taken a number of steps.

We were mentioning the tick size pilot before. We actually have, in our Division of Corporation Finance, an Office of Small Business Policy, which responds to a thousand-plus, sometimes nearly 2,000 requests for questions like how do I navigate the rules, how do I do this, how do I do that? They look at all of our rules from the perspective of how is this going to impact small businesses? So I think it is a very highly functioning unit.

I am an advocate for small business so, conceptually, I am all in favor of any advocate for small business because they are so important to our economy. I worry about—and I know our staff has given some technical assistance on this—but I worry, if the bill is adopted, that we might fragment or dilute the efforts that we have within the SEC.

Senator HEITKAMP. Chair White, I would submit that a lot of small business feel like they are being left behind and their capitalization is restricted in ways that they do not understand. And it is so critically important that they feel like they are part of the economic fabric as well. And so I think creating an advocacy so there is somebody there, and not just kind of the good will of the Chair and the good will of the rest of the Commission, to basically be that voice that is heard on small business concerns. So—

Ms. WHITE. I certainly understand the priority on it, if I can say it that way. I think that is why we have the office we have, but I also understand the priority that you are putting on it in this way, as well.

Senator HEITKAMP. And I do not know if you have had a chance to answer questions about the Department of Labor fiduciary rule yet.

Ms. WHITE. Here and there I have, yes.

[Laughter.]

Senator HEITKAMP. Yeah, I bet you have, so I will just kind of read the testimony there rather than reiterate what has been said.

The SEC is credited—has been credited for developing and adopting a March 2012 Current Guidance on Economic Analysis, an SEC rulemaking which emphasizes the importance of rigorous economic analysis and rulemaking, including relevant cost benefits. It is generally recognized that accurately estimating the benefits of regulation is more difficult than determining the costs, whether or not they can be quantified or monetized.

What lessons learned, if any, can you provide on SEC's efforts to justify regulations, especially when these limitations exist?

Ms. WHITE. Well, we obviously adopted and implemented our Economic Guidance. I think it was March of 2012. We take the cost-benefit economic analysis of our rules and pre-our rules quite seriously. And I think it is working very well. We have actually received compliments on the thoroughness of it and the pointedness of it, if I can say it that way.

So I think it is enormously important to do. And I will not say much about it but you alluded to the bills that are pending to add more review and other factors. What I worry about there is the compromise of independence and adding burdens that, at least at the SEC, I think we are discharging what you want us to.

Senator HEITKAMP. Chair White, I am running out of time, but I just want to reiterate that, you know, we can all have good intentions but sometimes we need a cop on the beat who is going to be reviewing the work.

And so that is really what we are asking for in that legislation. And we will continue to talk about what makes the independent agencies comfortable as we move forward, but I have not given up on my challenge of making sure that there is some oversight that assists this body in terms of oversight on independent agency regulations.

So, thank you so much for appearing and thank you for your work. I think if you have not been thanked already, as you know I am greatly appreciative that you have stepped up and taken the chair.

Ms. WHITE. Thank you very much. Thank you.

Chairman SHELBY. Senator Brown.

Senator BROWN. I have one last question. Thank you, Mr. Chairman.

First, one real brief comment. I join Schumer—Senator Schumer's plea with you to move on that. I think it is—I think there is a huge majority of the country, people paying attention, that want you to do that, and so many Members of this Committee too.

Along with other members of both houses, I sent you a letter in March asking you to consider rulemaking pursuant to a petition that would provide enhanced disclosure of the diversity of board nominees. In your response, you indicated you had asked your staff to look at the nature of the disclosure companies are providing. Could you give this Committee an update on what you are doing?

Ms. WHITE. Yes. And this is an example of an existing rule that we have that investors have basically indicated is not providing them useful enough information on diversity. There is no definition of diversity, et cetera. So those concerns resonate with me and I have had the Division of Corporation Finance work on what the disclosures have been in the past, what they are now, and how we might enhance that rule. They have not completed that process, but they are well into it, and I expect them to make a recommendation to me fairly soon.

Senator BROWN. Please keep me apprised of those findings.

Ms. WHITE. Absolutely.

Senator BROWN. Thank you.

Thank you, Mr. Chairman.

Chairman SHELBY. We appreciate your appearance today here, and we look forward to some more. Thank you.

Ms. WHITE. Thank you very much. Thank you.

Chairman SHELBY. The meeting is adjourned.

[Whereupon, at 10:57 a.m., the hearing was adjourned.]

[Prepared statements and responses to written questions supplied for the record follow:]

**PREPARED STATEMENT OF MARY JO WHITE**  
**CHAIR, SECURITIES AND EXCHANGE COMMISSION**  
**JUNE 14, 2016**

Testimony on “Oversight of the U.S. Securities and Exchange Commission”  
 by  
**Chair Mary Jo White**  
**U.S. Securities and Exchange Commission**  
 Before the  
**Committee on Banking, Housing, and Urban Affairs**  
**United States Senate**  
**June 14, 2016**

Chairman Shelby, Ranking Member Brown, and Members of the Committee:

Thank you for inviting me to testify today regarding the current work and initiatives of the U.S. Securities and Exchange Commission (SEC or Commission).<sup>1</sup> The SEC is a critical agency that serves as the bulwark safeguarding millions of investors and the most vibrant markets in the world. Thanks to the exceptional work and commitment of our superb staff, the Commission has in recent years strengthened its operations and programs across the agency – aggressively enforcing the securities laws to punish wrongdoers, adopting strong measures that protect investors and our markets, and investing in the people and technology required to ensure that our markets remain the strongest and safest in the world. These and other efforts across our extensive areas of responsibility are all in furtherance of our essential mission: to protect investors; to maintain fair, orderly, and efficient markets; and to facilitate capital formation.

The Commission’s actions and accomplishments since I testified before this Committee in September 2014 have been extensive.<sup>2</sup> Each of the last three years has been marked by vigorous enforcement and examination programs, empowered with new tools and methods to detect and hold wrongdoers accountable and protect investors. In fiscal year 2015 alone, the Commission brought over 800 enforcement actions, an unprecedented number; secured over \$4 billion in orders directing the payment of penalties and disgorgement, an all-time high; performed approximately 2,000 exams, a five-year high; and, even more importantly, continued to develop cutting-edge cases and smarter, more efficient exams. Aided by enhanced technology to analyze suspicious activity and strengthened by initiatives like self-reporting, SEC staff has been able to identify and target the most significant risks for investors across the market.

The Commission over the last three years has pursued very consequential rulemaking and other measures designed to protect investors, strengthen the markets, and open new avenues for capital-raising. Since I last testified, the agency, for example, has advanced major rules addressing important equity market structure issues – including controls on the technology used by key market participants, the transparency of alternative trading systems, and the consolidated

<sup>1</sup> The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the President, the full Commission, or any Commissioner.

<sup>2</sup> See generally *SEC Accomplishments: Protecting Investors and Our Markets Through Rigorous Oversight, Vigorous Enforcement, and Transformative Rulemaking* (June 13, 2016), available at <https://www.sec.gov/about/sec-accomplishments.htm>.

audit trail – while moving forward with a comprehensive assessment of other fundamental structural questions. We also issued a series of proposals to address the increasingly complex portfolios and operations of mutual funds and exchange-traded funds (ETFs). We adopted new rules for crowdfunding and smaller securities offerings under Regulation A, while proposing additional avenues for small businesses to raise capital. We finalized critical components of the regulatory regime for security-based swaps. We also proposed the full suite of rules regarding executive compensation practices. And we continued to execute a comprehensive review of the effectiveness of our disclosure regime.

This work, which is described in greater detail below, marks the latest phase of an extraordinary regulatory effort by the agency since before I became Chair, enlisting all of our policy divisions and offices. Beyond our discretionary initiatives, the Commission has now adopted final rules for 66 of the 86 mandatory rulemaking provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) directed to the SEC, the majority of them since I became Chair.<sup>3</sup> We have completed all of the rulemakings directed by the Jumpstart Our Business Startups Act (JOBS Act). And we have made significant progress advancing the rulemakings required of us late last year under the Fixing America's Surface Transportation Act (FAST Act). Some of the most significant initiatives of the last three years include:

- *Equity Market Structure.* An imperative of our modern equity markets is strong technological systems and operations, and the Commission has adopted Regulation Systems Compliance and Integrity (SCI) to require critical market participants – including exchanges, clearing agencies, and large alternative trading systems (ATSS) – to implement wide-ranging measures designed to reduce the occurrence of systems issues and improve resilience when such issues do occur. The self-regulatory organizations (SROs), acting under Commission oversight, have also continued to develop further measures to enhance the operational integrity of the markets. In addition, the Commission has proposed new rules to enhance market transparency, with the first-ever major update of Regulation ATS, and I expect that we will very soon propose rules requiring important new disclosures for how investor orders are handled by broker-dealers. The Commission has also proposed enhancements to our core regulatory tools of registration and firm oversight. And we have put out for notice and comment the final plan for the consolidated audit trail, as well as expanded our consideration of additional market structure reforms through the establishment of the Equity Market Structure Advisory Committee.
- *Money Market Funds and Asset Management.* To address the risk of investor runs, as experienced during the financial crisis, the Commission in 2014 adopted rules that fundamentally change the way money market funds operate, rules that will become fully operational this coming October. Following that work, the Commission undertook to enhance its regulatory regime for the broader asset management industry. In furtherance

<sup>3</sup> The current status of the Commission's implementation of the Dodd-Frank Act is summarized at <https://www.sec.gov/spotlight/dodd-frank.shtml>.

of that goal, the Commission last year proposed four major rules to address potential risks in the modern asset management industry, including rules that would improve and expand the information reported to the Commission and investors, impose new controls on how funds manage their liquidity, and enhance the regulation of funds' use of derivatives.

- *Capital Formation.* Implementing mandates from the JOBS Act, the Commission adopted rules to increase access to capital for smaller companies by revamping and enhancing Regulation A, and other rules to permit companies to offer and sell securities through equity crowdfunding. Separately, the Commission has also proposed rules to facilitate intrastate and regional securities offerings, including offerings relying upon recently adopted intrastate crowdfunding provisions under state securities laws. We also worked with the SROs to build a pilot program to widen the minimum quoting and trading increments – or tick sizes – for stocks of some smaller companies, which should aid in understanding whether wider tick sizes enhance the market quality and secondary liquidity of these stocks. This work follows on the Commission's adoption of rules to allow general solicitation for certain offers and sales made under Rule 506, as well as a rule to disqualify certain felons and other "bad actors" from participating in private securities offerings made under Rule 506.
- *Disclosure Effectiveness.* The staff of the Commission has undertaken a comprehensive assessment of the effectiveness of our disclosure regime for investors and issuers. As part of that assessment, the Commission issued a major concept release that seeks input on modernizing certain business and financial disclosure requirements in Regulation S-K for the benefit of investors and companies. We also issued a request for comment for certain financial reporting and disclosure requirements in final statements under Regulation S-X. I expect that the Commission will also shortly propose revisions to Industry Guide 7, which applies to disclosures about the projections and properties of mining companies.
- *Security-Based Swaps.* The Commission has implemented a substantial portion of a regulatory regime for security-based swaps required by the Dodd-Frank Act, which is designed to ensure that the \$11 trillion market for security-based swaps is safer, more transparent, and more efficient. Since I last testified, the Commission adopted the core rules for reporting security based swap transactions to regulators and the public through security-based swap data repositories. We also adopted the framework for registering security based swap dealers and major security-based swap participants with the Commission, as well as rules to help ensure that non-U.S. dealers participating in the U.S. market comply with our rules. Most recently, the Commission adopted extensive requirements for how these entities must conduct business with counterparties and acknowledge and verify their transactions. Finalizing the remainder of the rules for trade reporting and dealers activities – and operationalizing those regimes – is a priority for 2016.
- *Asset-Backed Securities.* The Commission in 2014 adopted wide-ranging rules to enhance transparency and better protect investors in the asset-backed securities market.

The Commission completed rules requiring significant enhancements to registered offering disclosures for asset-backed securities, a market with \$4.8 trillion in issuances over the past decade that stood at the epicenter of the financial crisis. Since I last testified, acting jointly with five other federal agencies, the Commission also adopted credit risk retention rules, which require securitizers of asset-backed securities to keep “skin in the game” for the securities they package and sell.

- *Executive Compensation.* In 2015, the Commission adopted the rule mandated by the Dodd-Frank Act requiring a company to disclose the ratio of compensation of its chief executive officer to the median compensation of its employees. The Commission in 2015 also proposed the remaining executive compensation rules required by the Dodd-Frank Act, including disclosure of whether a company allows executives to hedge the company’s stock, disclosure of pay versus performance measures of executive compensation, and new disclosures and rules for clawing back incentive compensation erroneously awarded. We also in 2016 re-proposed, jointly with other regulators, rules regarding disclosure and restrictions for certain incentive-based compensation arrangements at large financial institutions.
- *Credit Rating Agencies and Credit Ratings.* The Commission has adopted a comprehensive package of reforms in 2014 for the regulation and oversight of credit ratings agencies, including new controls on the management of conflicts of interest. The Commission has also acted to remove almost all of the references to credit ratings from its rules and forms.
- *Broker-Dealer Financial Responsibility.* The Commission, soon after I became Chair, adopted rules to provide additional safeguards with respect to a broker-dealer’s custody of customer securities and cash, as well as to strengthen the audit requirements for broker-dealers. In addition, the Commission adopted amendments to the broker-dealer financial responsibility rules to enhance protections for customer assets, firm capital requirements, and risk management controls. In 2016, we proposed, jointly with the Federal Deposit Insurance Corporation (FDIC), rules that implement procedures for the orderly liquidation of covered broker-dealers.
- *Municipal Advisors.* The Commission has established a new regulatory regime to protect municipalities and investors from conflicted advice and unregulated advisors by requiring municipal advisors to register with the SEC and to comply with the rules of the Municipal Securities Rulemaking Board (MSRB). And we continue to work with the MSRB to establish the full suite of regulatory obligations for municipal advisors.
- *Volcker Rule.* The Commission, in December 2013, adopted, jointly with other regulators, rules to implement a prohibition on proprietary trading and certain relationships with hedge funds and private equity funds. Compliance with those rules was required in 2015, and the SEC is now working in coordination with the other financial regulators to ensure that firms have taken the necessary steps.

While our work in enforcement and rulemaking are perhaps the most prominent examples of the agency's achievements, the imperatives of our mission are carried forward each day by all of the dedicated staff of our divisions and offices. The Division of Corporation Finance, for example, reviews the annual and periodic reports of thousands of issuers each year, helping to ensure that investors receive full and fair disclosure about the public companies in which they invest. And staff in the Office of Small Business Policy alone responded last year to over a thousand inquiries from small businesses about their questions and concerns. During the same period, the Division of Trading and Markets reviewed more than 2,100 filings from exchanges and other SROs to preserve a fair and orderly marketplace for all investors. The Division of Investment Management reviewed filings last year covering more than 12,500 mutual funds and other investment companies, where many individuals invest their hard-earned money to save for retirement, college, and other important goals. Our economists in the Division of Economic and Risk Analysis produced more than 30 incisive papers and publications in 2015, including two major analyses to help inform our work on asset management. And the numbers are only a small part of the story. Each instance of such engagement makes our markets better and safer for investors.

Throughout the agency, we are increasingly harnessing technology to better identify risks, uncover frauds, sift through large volumes of data, inform policymaking, and streamline operations. The Commission's emphasis on technological improvements is continuing to pay dividends, improving efficiencies while allowing us to cover more ground than ever before. We continue to build on this progress by seeking sufficient appropriated funds for a number of key information technology (IT) initiatives, including improvements to the Electronic Data Gathering, Analysis and Retrieval (EDGAR) system and our enforcement surveillance tools.

While the Commission today is stronger and more effective than ever before, challenges remain if we are to continue our current trajectory and address the growing size and complexity of the securities markets. We now oversee approximately 28,000 market participants and selectively review the disclosures and financial statements of over 9,000 reporting companies. From 2001 to 2015, assets under management of SEC-registered advisers more than tripled from approximately \$21.5 trillion to approximately \$66.8 trillion, and assets under management of mutual funds more than doubled from \$7 trillion to over \$15 trillion. Trading volume in the equity markets from 2001 through 2015 nearly tripled to over \$70 trillion. And, as this Committee knows, the SEC's responsibilities have also significantly increased, with new or expanded responsibilities for security-based derivatives, hedge fund and other private fund advisers, credit rating agencies, municipal advisers, clearing agencies, and crowdfunding portals. As I have testified before both the House and Senate, the SEC is significantly under-resourced for the extensive responsibilities it has, even though our budget is deficit neutral and funded by very modest transaction fees.

It is critical that we have the resources necessary to discharge our responsibilities, both the new ones and the many others we have long held in the face of a growing and ever-more sophisticated financial services industry. I deeply appreciate the serious charge we have to be prudent stewards of the funds we are appropriated, and we strive to demonstrate how seriously we take that obligation by the work we do. At the same time, the cuts and limitation to the SEC's budget that some have proposed would imperil the progress we have made and our ability

to fulfill our mission. Only with Congress' continued assistance can we continue to successfully execute our mission to protect investors, preserve the integrity of our markets, and promote capital formation. We very much appreciate the Committee's support.

#### **Vigorously Enforcing the Securities Laws**

The SEC's vigorous enforcement program is at the heart of our efforts to protect investors and instill confidence in the integrity of the markets. The Division of Enforcement (Enforcement) advances these efforts by investigating and bringing civil charges against violators of the federal securities laws. Successful enforcement actions impose meaningful sanctions on securities law violators, result in penalties and disgorgement of ill-gotten gains that can be returned to harmed investors, and deter future wrongdoing.

Enforcement delivered very strong results on behalf of investors in FY 2014, FY 2015 and continues to do so in FY 2016. The SEC filed a record 807 enforcement actions in FY 2015 covering a wide range of misconduct, and obtained orders totaling \$4.19 billion in disgorgement and penalties, both at record levels. Of the 807 enforcement actions, a record 507 were independent actions for violations of the federal securities laws, and 300 were either actions against issuers who were delinquent in making required filings with the SEC or administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders.

Even more important than the numbers, these actions addressed many of the most important issues for investors and markets, spanned the securities industry, and included numerous "first-of-their-kind" actions. Significantly, approximately two-thirds of our substantive actions in FY 2015 also included charges against individuals. A few other important features of our enforcement program also bear highlighting.

#### *Executing the Admissions Policy*

The Commission continues to use its first of its kind admissions policy to aggressively seek admissions in certain cases where heightened accountability and acceptance of responsibility by a defendant is particularly important and in the public interest. These types of cases include those involving particularly egregious conduct; where large numbers of investors were harmed; where the markets or investors were placed at significant risk; where the conduct undermines or obstructs our investigative process; where an admission can send an important message to the markets; or where the wrongdoer presents a particular future threat to investors or the markets. Since implementing the admissions protocol in 2013, the SEC has obtained admissions from over 50 entities and individuals, including major financial institutions and national auditing firms. We also required individuals to admit wrongdoing in a number of cases, including a world-wide pyramid scheme targeting the Asian-American community.<sup>4</sup> While this

<sup>4</sup> We also do not accept "neither admit nor deny" settlements where a defendant has acknowledged relevant facts in a settlement with other criminal or civil authorities, or been convicted. This regularly occurs in connection with

is an evolving protocol that continues to be applied to more cases, as we indicated when we implemented it, the majority of cases will continue to be resolved on a “neither admit nor deny” basis, which is the norm for other civil law enforcement agencies and in private litigation.<sup>5</sup> We are committed, however, to requiring admissions where appropriate, and are prepared to litigate those cases if necessary.

#### *Enhancing Focus on Key Areas of Misconduct*

The Commission also continues to focus resources on key areas of misconduct. One critical area is financial reporting and issuer disclosure. Comprehensive, accurate, and reliable financial reporting is the bedrock upon which our markets are based, and is essential to ensuring public confidence in them. And at my direction, since 2013, our Enforcement Division has intensified its focus on pursuing violations in this area. Part of this effort involved creating a dedicated group of accountants, attorneys, and analysts who use cutting edge data analytical tools to look for evidence of reporting discrepancies and other early warning signs of financial reporting fraud. The SEC brought a series of significant financial reporting cases in FY 2015, including four emblematic actions last September, each of which involved sophisticated

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guilty pleas that arise from parallel criminal investigations, which frequently are matters that we referred to a criminal prosecutor in which our own investigation assisted in securing a favorable resolution on the criminal side as well. While these cases are not included in the admissions cited above, they serve the same purpose and have the same impact. We have obtained these kinds of settlements with dozens of individuals and entities since this policy changed at the end of 2011.

<sup>5</sup> In the majority of its cases, the Commission, like all other federal agencies with civil law enforcement powers, determines that it is appropriate to continue to settle on a “no admit, no deny” basis. This practice allows the Commission to obtain significant relief, eliminate litigation risk, return money to victims more expeditiously, and conserve enforcement resources for other matters. But, in 2013, we determined that our Enforcement program’s deterrent message could be enhanced by requiring admissions of wrongdoing in appropriate cases. We are pleased to see that other civil law enforcement agencies have begun to follow our lead. For example, the CFTC requires admissions in certain cases and entered into its first admissions settlement in October 2013. See Release PR6737-13, *CFTC Files and Settles Charges Against JPMorgan Chase Bank, N.A., for Violating Prohibition on Manipulative Conduct In Connection with “London Whale” Swaps Trades*, Oct. 16, 2013, <http://www.cftc.gov/PressRoom/PressReleases/pr6737-13> [Max Stendahl, *CFTC Mimics SEC Policy Shift With JPMorgan ‘Whale’ Pact*, Law360 (Oct. 16, 2013, 7:47 p.m.), <http://www.law360.com/articles/480686/cftc-mimics-sec-policy-shift-with-jpmorgan-whale-pact>]. Similarly, the CFPB requires admissions in certain cases and entered into its first admissions settlement in February 2014. See Press Release, *CFPB Takes Action Against Mortgage Lender for Illegal Payments*, Feb. 24, 2014, <http://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-mortgage-lender-for-illegal-payments/>.

disclosure violations or cleverly masked reporting fraud.<sup>6</sup> Each of these cases also involved charges against senior executives. Holding individuals accountable for their role in financial misconduct is a significant priority of mine and in FY 2015, we charged 120 individuals in our substantive issuer reporting and disclosure cases, approximately twice the number of individuals we charged in FY 2014.

Another key area of enforcement is investment management, where the SEC has continued to bring actions addressing a widening range of issues, including performance advertising, undisclosed conflicts of interest, compliance issues, and private equity fees and expenses. Among these are “first-of-their-kind” actions for failures to report material compliance matters to fund boards and the improper allocation of expenses by private equity advisers. The Enforcement Division’s focus on private equity has expanded significantly over the past few years and, to date, the SEC has brought eight enforcement actions related to private equity advisers breaching their fiduciary duties by charging undisclosed fees and expenses, shifting and misallocating expenses, and failing to adequately disclose conflicts of interest.

In addition, since I last testified before the Committee, Enforcement has emphasized market structure issues, bringing significant enforcement actions involving high frequency trading, the operation of trading platforms such as dark pools, manipulative trading, and market access and technology controls. We have brought cases, for example, against ATSs for misusing confidential customer trading information, actions against high frequency traders for manipulative trading and net capital violations, and against exchanges for providing some, but not all, traders with additional information about certain order types.

#### *Enhancing the Whistleblower Program*

The SEC’s Whistleblower program continues to have a transformative impact on our enforcement program. The SEC’s Office of the Whistleblower is currently tracking hundreds of matters in which a whistleblower’s tip has caused a matter under investigation or an investigation to be opened, or which have been forwarded to Enforcement staff for consideration in connection with an existing investigation. The number of whistleblower tips received by the Commission has increased each year of the program’s operation. In Fiscal Year 2015, the Commission received nearly 4,000 whistleblower tips, representing a 30% increase over the number of tips received in Fiscal Year 2012, the first year for which the office had full-year data. In FY 2015, the Commission paid more than \$37 million to whistleblowers who provided original information that led to successful enforcement actions resulting in an order or monetary

<sup>6</sup> See Press Release No. 2015-184, *SEC Charges BDO and Five Partners in Connection With False and Misleading Audit Opinions* (Sept. 9, 2015), available at <https://www.sec.gov/news/pressrelease/2015-184.html>; Press Release No. 2015-179, *SEC Charges Sports Nutrition Company With Failing to Properly Disclose Perks for Executives* (Sept. 8, 2015) available at <https://www.sec.gov/news/pressrelease/2015-179.html>; Press Release No. 2015-180, *SEC Charges Bankrate and Former Executives With Accounting Fraud* (Sept. 8, 2015), available at <https://www.sec.gov/news/pressrelease/2015-180.html>; and Press Release No. 2015-183, *SEC Charges Video Management Company Executives With Accounting Fraud* (September 8, 2015), available at <https://www.sec.gov/news/pressrelease/2015-183.html>.

sanctions exceeding \$1 million, and has awarded more than \$50 million since the program's inception. Just last week, the Commission announced a \$17 million award, its second largest, to a former company employee whose detailed tip substantially advanced Enforcement's investigation. The Commission has also filed numerous "friend of the court" briefs in support of private actions by whistleblowers who have experienced retaliation for reporting internally at their companies, and has brought our own actions against firms for whistleblower retaliation and improper restrictions of whistleblowing activity in confidentiality agreements.

#### *Preserving Investigative Tools*

During my tenure as Chair, I have sought to work with Congress to modernize the Electronic Communications Privacy Act (ECPA), which governs the authority of law enforcement to obtain emails from internet service providers (ISPs). The bills currently pending in Congress to amend ECPA would unfortunately pose significant risks to the American investing public by impeding the ability of Commission staff to investigate and uncover insider trading, Ponzi schemes, and other types of fraud. Although I agree that ECPA's privacy protections and evidence collection procedures should be updated, I believe there are ways to update ECPA that offer stronger privacy protections and observe constitutional boundaries without putting innocent victims and our capital markets at risk.

As drafted, the bills would require government entities to obtain a criminal warrant when they seek the content of subscriber emails and other electronic communications from ISPs. The SEC, as a civil law enforcement agency, cannot obtain criminal warrants. Thus, the SEC would no longer be able to gather these communications directly from an ISP to obtain often critical and otherwise unobtainable evidence of serious wrongdoing. Any effort to update ECPA can, and should, be done without harming the ability of the SEC to protect our nation's citizens from securities fraud. I look forward to the opportunity to continue to work with Congress on solutions that both protect investors and privacy interests.

#### **Building Stronger, Safer Markets for Investors and Issuers**

The SEC continues to pursue an extensive program of rulemaking and other policy efforts designed to ensure that our securities markets continue to optimally and securely serve investors and issuers. Since I last testified before the Committee, the SEC has significantly progressed in implementing mandatory rulemakings under three separate statutes, as well as in pursuing an impressive range of important discretionary initiatives.

As the Committee knows, the SEC and our fellow regulators have been working hard to strengthen our nation's financial systems by implementing the rules mandated by the Dodd-Frank Act, which responded to the worst financial crisis since the Great Depression. Over the last two years, the SEC has moved into the final phase of implementing the Dodd-Frank Act, focusing on completing all of the remaining rules in the two major remaining areas of mandates: security-based swaps and executive compensation.

*Increasing Transparency and Oversight for Security-Based Swaps*

Since September 2014, we have marked several milestones in the establishment of a comprehensive regulatory framework for security-based swaps, which will give us powerful tools to oversee an \$11 trillion market. First, we finalized the core requirements for reporting security-based swap transactions to regulators and the public through security-based swap data repositories,<sup>7</sup> and we proposed additional requirements to ensure that reporting will produce accurate data for regulators and market participants.<sup>8</sup> With the adoption of these rules expected later this year, the regulatory infrastructure for transaction reporting will be complete.

Second, we adopted the framework for registering security-based swap dealers and major security-based swap participants with the Commission,<sup>9</sup> as well as rules to help ensure that non-U.S. dealers participating in the U.S. market comply with our rules.<sup>10</sup> Work is now underway to finalize the obligations that registered dealers and participants will be required to undertake. In April, the SEC adopted extensive requirements for how these entities must conduct business with counterparties – including special entities like municipalities and pension funds – and supervise such conduct.<sup>11</sup> We also this month finalized rules for timely and accurate trade acknowledgment and verification requirements for security-based swaps,<sup>12</sup> and have proposed a

<sup>7</sup> See Release No. 34-74246, *Security-Based Swap Data Repository Registration, Duties, and Core Principles* (February 11, 2015), available at <https://www.sec.gov/rules/final/2015/34-74244.pdf>; Release No. 34-74244, *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information* (February 11, 2015), available at <https://www.sec.gov/rules/final/2015/34-74244.pdf>.

<sup>8</sup> See Release No. 34-74245, *Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information* (February 11, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-74245.pdf>; Release No. 34-76624, *Establishing the Form and Manner with which Security-Based Swap Data Repositories Must Make Security-Based Swap Data Available to the Commission* (December 11, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-76624.pdf>; and Release No. 34-75845, *Access to Data Obtained by Security-Based Swap Data Repositories and Exemption from Indemnification Requirement* (September 4, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-75845.pdf>.

<sup>9</sup> See Release No. 34-75611, *Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants* (August 5, 2015), available at <https://www.sec.gov/rules/final/2015/34-75611.pdf>.

<sup>10</sup> See Release No. 34-77104, *Security-Based Swap Transactions Connected with a Non-U.S. Person's Dealing Activity That Are Arranged, Negotiated, or Executed By Personnel Located in a U.S. Branch or Office or in a U.S. Branch or Office of an Agent; Security-Based Swap Dealer De Minimis Exception* (Feb. 10, 2016), available at <https://www.sec.gov/rules/final/2016/34-77104.pdf>; and Release No. 34-72472, *Application of "Security-Based Swap Dealer" and "Major Security-Based Swap Participant" Definitions to Cross-Border Security-Based Swap Activities* (June 25, 2014), available at <https://www.sec.gov/rules/final/2014/34-72472.pdf>.

<sup>11</sup> See Release No. 34-77617, *Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants* (April 14, 2016), available at <https://www.sec.gov/rules/final/2016/34-77617.pdf>.

<sup>12</sup> See Release No. 34-78011, *Trade Acknowledgment and Verification of Security-Based Swap Transactions* (June 8, 2016), available at <https://www.sec.gov/rules/final/2016/34-78011.pdf>.

process for dealing with bad actors in the security-based swap market.<sup>13</sup> Next in line will be to finalize that process, complete capital, margin, and asset segregation requirements for security-based swap entities,<sup>14</sup> and adopt rules for recordkeeping and regulatory reporting.<sup>15</sup> With those steps, the regulatory structure for security-based swap dealers will be complete, a priority supported by all of the Commissioners.<sup>16</sup> Our goal is to finalize those rules by year-end.

#### *Creating New Disclosures and Limits for Executive Compensation*

With respect to executive compensation, the SEC last year issued proposals for all of the remaining executive compensation rulemakings required by the Dodd-Frank Act, including disclosure of whether a company allows executives to hedge the company's stock, disclosure of pay versus performance measures of executive compensation, and new disclosures and rules for clawing back incentive compensation erroneously awarded.<sup>17</sup> Together with five of our fellow financial regulators, we also re-proposed a joint rule regarding incentive-based compensation arrangements at large financial institutions.<sup>18</sup> The final rules are expected to be advanced expeditiously. And following the analysis of some 285,500 total comment letters, 1,500 of them unique, the final pay ratio rule was adopted in August 2015.<sup>19</sup>

<sup>13</sup> See Release No. 34-75612, *Applications by Security-Based Swap Dealers or Major Security-Based Swap Participants for Statutory Disqualified Associated Persons to Effect or Be Involved in Effecting Security-Based Swaps* (August 5, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-75612.pdf>.

<sup>14</sup> See Release No. 34-68071, *Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers* (October 18, 2012), available at <https://www.sec.gov/rules/proposed/2012/34-68071.pdf>.

<sup>15</sup> See Release No. 34-71958, *Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers* (April 17, 2014), available at <https://www.sec.gov/rules/proposed/2014/34-71958.pdf>.

<sup>16</sup> See Commissioner Daniel M. Gallagher and Commissioner Michael S. Piwowar, *Statement Regarding Security-Based Swap Rules* (Sept. 25, 2015), available at <https://www.sec.gov/news/statement/gallagher-piowar-security-based-swaps.html>; and Commissioner Kara M. Stein, *Remarks at the "SEC Speaks" Conference* (February 19, 2016), available at <https://www.sec.gov/news/speech/stein-sec-speaks-2016.html>.

<sup>17</sup> See Release No. 33-9723, *Disclosure of Hedging by Employees, Officers and Directors* (February 9, 2015), available at <https://www.sec.gov/rules/proposed/2015/33-9723.pdf>; Release No. 34-74835, *Pay Versus Performance* (April 29, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-74835.pdf>; and Release No. 33-9861, *Listing Standards for Recovery of Erroneously Awarded Compensation* (July 1, 2015), available at <https://www.sec.gov/rules/proposed/2015/33-9861.pdf>.

<sup>18</sup> See Release No. 34-77776, *Incentive-based Compensation Arrangements* (May 6, 2016), available at <https://www.sec.gov/rules/proposed/2016/34-77776.pdf>.

<sup>19</sup> See Release No. 33-9877, *Pay Ratio Disclosure* (August 5, 2015), available at <https://www.sec.gov/rules/final/2015/33-9877.pdf>.

*Completing Implementation of the Dodd-Frank Act*

Beyond these two areas, the SEC has continued to finish all of the mandates of the Dodd-Frank Act since I last testified. As required by Section 1504, we re-proposed rules that would require resource extraction issuers to disclose payments made to the U.S. federal government or foreign governments for the commercial development of oil, natural gas, or minerals.<sup>20</sup> And, working with our colleagues at the FDIC, we proposed joint rules for broker-dealers covered under the orderly liquidation provisions of Title II, as required by Section 205(h) of the Dodd-Frank Act.<sup>21</sup>

These accomplishments of the last two years were, of course, only the latest in an historic undertaking by the agency to execute the most daunting rulemaking agenda in memory. Pursuant to mandates of the Dodd-Frank Act, since I arrived at the agency in April 2013, we have stood up an entirely new regulatory regime for municipal advisors,<sup>22</sup> and implemented sweeping changes in the securitization markets that were at the epicenter of the crisis – including the joint rulemaking on credit risk retention since I last testified before the Committee.<sup>23</sup> We significantly enhanced the rules for credit rating agencies,<sup>24</sup> strengthened the rules for how broker-dealers handle customer funds and securities,<sup>25</sup> disqualified bad actors from private offerings,<sup>26</sup> removed credit rating references from throughout our rules,<sup>27</sup> and, through the Volcker Rule, restricted proprietary trading by financial institutions.<sup>28</sup>

<sup>20</sup> See Release No. 34-76620, *Disclosure of Payments by Resource Extraction Issuers* (December 11, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-76620.pdf>.

<sup>21</sup> See Release No. 34-77157, *Covered Broker-Dealer Provisions under Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (February 17, 2016), available at <https://www.sec.gov/rules/proposed/2016/34-77157.pdf>.

<sup>22</sup> See Release No. 34-70462, *Registration of Municipal Advisors* (September 30, 2013), available at <https://www.sec.gov/rules/final/2013/34-70462.pdf>.

<sup>23</sup> See Release No. 34-73407, *Credit Risk Retention* (October 22, 2014), available at <https://www.sec.gov/rules/final/2014/34-73407.pdf>; and Release No. 33-9638, *Asset-Backed Securities Disclosure and Registration* (September 4, 2014), available at <https://www.sec.gov/rules/final/2014/33-9638.pdf>.

<sup>24</sup> See Release No. 34-72936, *Nationally Recognized Statistical Rating Organizations* (August 27, 2014), available at <https://www.sec.gov/rules/final/2014/34-72936.pdf>.

<sup>25</sup> See Release No. 34-70073, *Broker-Dealer Reports* (July 30, 2013), available at <https://www.sec.gov/rules/final/2013/34-70073.pdf>. In addition, the Commission adopted amendments to the broker-dealer financial responsibility rules to enhance protections for customer assets, firm capital requirements, and risk management controls and proposed rules to provide investors with useful information about modern broker-dealer order handling practices. See Release No. 34-70072, *Financial Responsibility Rules for Broker-Dealers* (July 30, 2013), available at <https://www.sec.gov/rules/final/2013/34-70072.pdf>.

<sup>26</sup> See Release No. 33-9414, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings* (July 10, 2013), available at <https://www.sec.gov/rules/final/2013/33-9414.pdf> ("Bad Actor Rule").

<sup>27</sup> See Release No. IC-31828, *Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule* (September 16, 2015), available at <https://www.sec.gov/rules/final/2015/ic-31828.pdf>; Release No. IC-30847, *Removal of Certain References to Credit*

### Facilitating Capital Formation for both Large and Small Issuers

The SEC performs a critical function for issuers seeking to raise capital to grow their businesses and the larger economy. Our rules must facilitate offerings by a diverse set of companies – large and small, engaged in all manner of commerce – while ensuring that investors have the protections they require to maintain confidence in the strongest capital markets in the world. Since I last testified before this Committee, the SEC has concentrated our commitment to this responsibility through a number of key initiatives, with particular emphasis on smaller businesses.

#### *Completing Implementation of the JOBS Act and the FAST Act*

The JOBS Act, in particular, made several significant changes to the avenues for capital formation in the securities markets, especially for smaller issuers, and we have now completed all of the rules mandated by that legislation. A few months after I became Chair, we finalized the changes to private offerings required by the JOBS Act, while advancing measures to ensure the agency has the information it needs to monitor the changes and protect investors.<sup>29</sup> Last year, the SEC adopted final rules to update and expand Regulation A (commonly referred to as Regulation A+), an exemption from registration for small offerings of securities, to facilitate smaller companies' access to capital.<sup>30</sup> And we also finalized new rules to permit securities-based crowdfunding offerings by issuers and the operation of funding portals to intermediate such offerings.<sup>31</sup> Issuers are now actively using both of these new avenues for raising capital.

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*Ratings Under the Investment Company Act* (December 27, 2013), available at <https://www.sec.gov/rules/final/2013/33-9506.pdf>; and Release No. 34-71194, *Removal of Certain References to Credit Ratings Under the Securities Exchange Act of 1934* (December 27, 2013), available at <https://www.sec.gov/rules/final/2013/34-71194.pdf>.

<sup>28</sup> See Release No. BHCA-1, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests In, and Relationships With, Hedge Funds and Private Equity Funds* (December 10, 2013), available at <https://www.sec.gov/rules/final/2013/bhca-1.pdf>; and Release No. BHCA-2, *Treatment of Certain Collateralized Debt Obligations Backed Primarily by Trust Preferred Securities with Regard to Prohibitions and Restrictions on Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds* (January 17, 2014), available at <https://www.sec.gov/rules/interim/2014/bhca-2.pdf>.

<sup>29</sup> See Release No. 33-9415, *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings* (July 10, 2013), available at <https://www.sec.gov/rules/final/2013/33-9415.pdf>; and Release No. 33-9416, *Amendments to Regulation D, Form D and Rule 156 under the Securities Act* (July 10, 2013), available at <https://www.sec.gov/rules/proposed/2013/33-9416.pdf>. On the same day, the Commission adopted rules to disqualify certain felons and other “bad actors” from participating in securities offerings made under Rule 506. See *Bad Actor Rule*, *supra* note 26.

<sup>30</sup> See Release No. 33-9741, *Amendments for Small and Additional Issues Exemptions under the Securities Act (Regulation A)* (March 25, 2015), available at <https://www.sec.gov/rules/final/2015/33-9741.pdf>.

<sup>31</sup> See Release Nos. 33-9974; 34-76324, *Crowdfunding* (October 30, 2015), available at <https://www.sec.gov/rules/final/2015/33-9974.pdf>.

The FAST Act was enacted by Congress late last year, requiring the SEC to undertake several more rules and studies to promote capital formation and modernize disclosure. We have already made progress on implementing those mandates, adopting interim final rules to revise registration forms for emerging growth companies and smaller reporting companies,<sup>32</sup> and to permit issuers to include a summary in the annual report on Form 10-K.<sup>33</sup> Earlier this year, the SEC also approved amendments to revise the rules related to the thresholds for registration, termination of registration, and suspension of reporting under Section 12(g) of the Securities Exchange Act, implementing provisions of both the JOBS and the FAST Acts.<sup>34</sup>

*Creating New Opportunities for Smaller Issuers*

The Commission has gone beyond the statutory mandates since I last testified and also developed and adopted a number of additional initiatives that are designed to facilitate capital formation, particularly for small businesses. In October 2015, for example, the Commission issued a rule proposal seeking to modernize Rule 147, a safe harbor to a statutory exemption for intrastate securities offerings, which would establish a new exemption to facilitate capital formation through intrastate offerings.<sup>35</sup> Many market participants and state regulators had raised concerns that the current requirements have not kept up with changes in the business environment and technology, which limits the usefulness of the safe harbor for capital-raising, especially for smaller state and local businesses. The rule proposal would retain the key feature of existing Rule 147 – its intrastate character, which permits companies to raise money from investors within their state without concurrently registering the offers and sales at the federal level. In recognition of the transformative nature of the internet and other technologies, however, the rule would, among other things, remove the existing intrastate restriction on offers, but – critically for the state-based nature of the offering and its regulation – would continue to require that sales be made only to residents of the state or territory of the issuer's principal place of business. The proposal would also modify and modernize some of the issuer eligibility requirements to make the rule available to a greater number of businesses seeking financing in-

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<sup>32</sup> See Release No. 33-10003, *Simplification of Disclosure Requirements for Emerging Growth Companies and Forward Incorporation by Reference on Form S-1 for Smaller Reporting Companies* (January 13, 2016), available at <https://www.sec.gov/rules/interim/2016/33-10003.pdf>.

<sup>33</sup> See Release No. 34-77969, *Form 10-K Summary* (June 1, 2016), available at <https://www.sec.gov/rules/interim/2016/34-77969.pdf>.

<sup>34</sup> See Release No. 33-10075, *Changes to Exchange Act Registration Requirements to Implement Title V and Title VI of the JOBS Act* (May 3, 2016), available at <https://www.sec.gov/rules/final/2016/33-10075.pdf>.

<sup>35</sup> See Release No. 33-9973, *Exemptions to Facilitate Intrastate and Regional Securities Offerings* (October 30, 2015), available at <https://www.sec.gov/rules/proposed/2015/33-9973.pdf>.

state, while requiring that such financing occur with a set of certain investor protections and that issuers have a sufficient in-state presence within the state of offering.<sup>36</sup>

Another important initiative is the pilot program to widen the minimum quoting and trading increments – or tick sizes – for stocks of some smaller companies. Following a study directed by the JOBS Act,<sup>37</sup> the Commission in May 2015 approved a proposal, submitted in response to a Commission order,<sup>38</sup> by the national securities exchanges and the Financial Industry Regulatory Authority (FINRA) for a two-year pilot program.<sup>39</sup> The SEC plans to use the pilot program to assess whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors. The pilot is scheduled to begin on October 3, 2016.<sup>40</sup>

More broadly, the Commission staff remains committed to helping small issuers use these channels and others to build their businesses using the securities markets. The Office of Small Business Policy within the Division of Corporation Finance provides extensive guidance to small businesses seeking to raise capital or comply with our reporting requirements. Each year, the office responds to over 1,000 requests for interpretive advice, provides guidance through speaking engagements, and meets frequently with interested parties about pending rulemakings that could impact small businesses. The Commission also renewed the Advisory Committee on Small and Emerging Companies to provide the Commission with advice on capital formation and reporting requirements for smaller issuers.<sup>41</sup>

<sup>36</sup> While the proposed rule could be used for any intrastate offering meeting its conditions, more than 25 states have enacted some form of intrastate crowdfunding, and this provision could facilitate capital raising through those state provisions.

<sup>37</sup> *Report to Congress on Decimalization* (July 2012), available at <https://www.sec.gov/news/studies/2012/decimalization-072012.pdf>.

<sup>38</sup> See Release No. 34-72460, *Order Directing the Exchanges and the Financial Industry Regulatory Authority To Submit a Tick Size Pilot Plan* (June 24, 2014), available at <https://www.sec.gov/rules/other/2014/34-72460.pdf>.

<sup>39</sup> See Release No. 34-74892, *Joint Industry Plans; Order Approving the National Market System Plan to Implement a Tick Size Pilot Program* by BATS Exchange, Inc., BATS Y-Exchange, Inc., Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, The Nasdaq Stock Market LLC, New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc., as Modified by the Commission, *For a Two-Year Period* (May 6, 2015), available at <https://www.sec.gov/rules/sro/nms/2015/34-74892.pdf>.

<sup>40</sup> On November 6, 2015, the Commission issued an exemption to the Participants requiring implementation of the Tick Size Pilot until October 3, 2016. See Release No. 34-76382, *Order Granting Exemption from Compliance with the National Market System Plan to Implement a Tick Size Pilot Program* (November 6, 2015), available at <https://www.sec.gov/rules/exorders/2015/34-76382.pdf>.

<sup>41</sup> Information regarding the committee and its recommendations can be found at <https://www.sec.gov/info/smallbus/acsec.shtml>.

*Updating the Definition of an “Accredited Investor”*

In another important step for modernizing the private offering market, the Commission published a staff report in December 2015 regarding the key definition of “accredited investor,” which analyzes various approaches for modifying the definition and provides staff recommendations for potential updates and modifications.<sup>42</sup> The report recommends that the Commission consider expanding the definition to include alternative indicators for individuals to qualify as accredited investors (other than looking solely at income and net worth). The report also evaluates the impact that potential changes to the definition would have on the size of the accredited investor pool. I have directed the staff to prepare recommendations for the Commission on how the definition should be modified, and the comments we are receiving in response to the report will help inform the next steps.

**Strengthening Markets with Targeted Action and Data-Driven Analysis**

Since I last testified before this Committee, we have proceeded with our ongoing assessment of U.S. equity market structure to ensure that our markets remain the deepest, fairest, and most reliable in the world. It is important that our market structure is optimally serving investors and companies of all sizes seeking to raise capital. Our approach is data-driven and includes a number of identified short-term enhancements, as well as a comprehensive review of the entire structural operation of the equity markets to determine whether other changes should be made to optimize our markets for investors and issuers. The Commission staff has also continued to pursue efforts with FINRA and the MSRB to enhance the structure of the fixed income markets.

*Preserving Operational Integrity in the Equity Markets*

As I have remarked since my earliest days at the Commission,<sup>43</sup> a fundamental requirement of our modern equity markets is strong technological systems and operations. Shortly after my appearance at the September 2014 hearing of the Committee, the Commission adopted wide-ranging rules designed to strengthen the technology infrastructure of the U.S. securities markets.<sup>44</sup> The rules – together comprising Regulation SCI – impose requirements on

<sup>42</sup> See *Report on the Review of the Definition of “Accredited Investor”* (December 18, 2015), available at <https://www.sec.gov/corpfin/reportspublications/special-studies/review-definition-of-accredited-investor-12-18-2015.pdf>.

<sup>43</sup> See, e.g., Chair Mary Jo White, *Enhancing Our Equity Market Structure* (June 5, 2014) available at <https://www.sec.gov/News/Speech/Detail/Speech/1370542004312> (“Chair White Market Structure Framework Speech”); Chair Mary Jo White, *Focusing on Fundamentals: The Path to Address Equity Market Structure*, (October 2, 2013), available at <https://www.sec.gov/News/Speech/Detail/Speech/1370539857459>; and Chair Mary Jo White, *Statement on Meeting with Leaders of Exchanges* (September 12, 2013), available at <https://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539804861> (“Chair White Exchange Meeting Statement”).

<sup>44</sup> See Release No. 34-73639, *Regulation Systems Compliance and Integrity* (November 19, 2014) (“Regulation SCI Adopting Release”), available at <https://www.sec.gov/rules/final/2014/34-73639.pdf>.

certain key market participants intended to reduce the occurrence of systems issues and improve resiliency when systems problems do occur.

Our efforts to preserve the operational integrity of the market extend well beyond Commission rulemaking. In response to my requests,<sup>45</sup> the SROs have continued to work to address issues like order types and operations, data feed disclosures, and “single points of failure” within infrastructure systems that have the ability to significantly disrupt trading.<sup>46</sup> Most recently, the Commission approved new rules of the New York Stock Exchange, NYSE MKT, and Nasdaq that provide for closing contingency procedures for listed securities if the relevant exchange is unable to conduct a closing transaction in one or more securities due to a systems or technical issue.<sup>47</sup> All of the exchanges have now conducted and completed in-depth analyses of order types and have filed proposed rule changes to clarify the operation of their order types.<sup>48</sup> All of the exchanges have also now submitted rule filings disclosing how they use securities information processor (SIP) feeds and direct feeds.<sup>49</sup> These filings provide significantly

<sup>45</sup> See, e.g., Chair White Market Structure Framework Speech and Chair White Exchange Meeting Statement, *supra* note 43.

<sup>46</sup> See Chair Mary Jo White, *The Continuous Process of Optimizing the Equity Markets* (June 2, 2016), available at <https://www.sec.gov/news/speech/the-continuous-process-of-optimizing-the-equity-markets.html>.

<sup>47</sup> See Release No. 34-78015, *Notice of Filings of Amendment No. 1, and Order Granting Accelerated Approval of Proposed Rule Changes, as Modified by Amendment No. 1, to Provide for How the Exchanges Would Determine an Official Closing Price if the Exchanges are Unable to Conduct a Closing Transaction* (June 8, 2016), available at <http://www.sec.gov/rules/sro/nyse/2016/34-78015.pdf>; Release No. 34-78014, *Notice of Filing of Amendment No. 1, and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to Establish Secondary Contingency Procedures for the Exchange’s Closing Cross* (June 8, 2016), available at <http://www.sec.gov/rules/sro/nasdaq/2016/34-78014.pdf>.

<sup>48</sup> See Release Nos. 34-74796 (April 23, 2015), 80 Fed. Reg. 23,838 (April 29, 2015) (SR-NYSEArca-2015-08); 34-74738 (April 16, 2015), 80 Fed. Reg. 22,600 (April 22, 2015) (SR-BATS-2015-09); 34-74739 (April 16, 2015), 80 Fed. Reg. 22,567 (April 22, 2015) (SR-BYX-2015-07); 34-74558 (March 20, 2015), 80 Fed. Reg. 16,050 (March 26, 2015) (SR-NASDAQ-2015-024); 34-74618 (March 31, 2015), 80 Fed. Reg. 18,452 (April 6, 2015) (SR-Phlx-2015-29); 34-74617 (March 31, 2015), 80 Fed. Reg. 18,473 (April 6, 2015) (SR-BX-2015-015); 34-74439 (March 4, 2015), 80 Fed. Reg. 12,666 (March 10, 2015) (SR-EDGX-2015-08); 34-74435 (March 4, 2015), 80 Fed. Reg. 12,655 (March 10, 2015) (SR-EDGA-2015-10); 34-73468 (October 29, 2014), 79 Fed. Reg. 65,450 (November 4, 2014) (SR-EDGX-2014-18); 34-73592 (November 13, 2014), 79 Fed. Reg. 68,937 (November 19, 2014) (SR-EDGA-2014-20); 34-73572 (November 10, 2014), 79 Fed. Reg. 68,736 (November 18, 2014) (SR-CHX-2014-18); 34-74678 (April 8, 2015), 80 Fed. Reg. 20,053 (April 14, 2015) (SR-NYSE-2015-15); and 34-74682 (April 8, 2015), 80 Fed. Reg. 20,043 (April 14, 2015) (SR-NYSEMKT-2015-22).

<sup>49</sup> See Release Nos. 34-72685 (July 28, 2014), 79 Fed. Reg. 44,889 (August 1, 2014) (SR-BATS-2014-029); 34-72687 (July 28, 2014), 79 Fed. Reg. 44,926 (August 1, 2014) (SR-BYX-2014-012); 34-72682 (July 28, 2014), 79 Fed. Reg. 44,938 (August 1, 2014) (SR-EDGA-2014-17); 34-72683 (July 28, 2014), 79 Fed. Reg. 44,950 (August 1, 2014) (SR-EDGX-2014-20); 34-72711 (July 29, 2014), 79 Fed. Reg. 45,570 (August 5, 2014) (SR-CHX-2014-10); 34-72710 (July 29, 2014), 79 Fed. Reg. 45,511 (August 5, 2014) (SR-NYSE-2014-38); 34-72708 (July 29, 2014), 79 Fed. Reg. 45,572 (August 5, 2014) (SR-NYSEArca-2014-82); 34-72709 (July 29, 2014), 79 Fed. Reg. 45,513 (August 5, 2014) (SR-NYSEMKT-2014-62); 34-72684 (July 28, 2014), 79 Fed. Reg. 44,956 (August 1, 2014) (SR-NASDAQ-2014-072); 34-72713 (July 29, 2014), 79 Fed. Reg. 45,544 (August 5, 2014) (SR-Phlx-2014-49); 34-72712 (July 29, 2014), 79 Fed. Reg. 45,521 (August 5, 2014) (SR-BX-2014-037); 34-74074 (January 15, 2015), 80 Fed. Reg. 3,679 (January 23, 2015) (SR-BATS-2015-04); 34-74075 (January 15, 2014), 80 Fed. Reg. 3,693 (January 23, 2015) (SR-BYX-2015-03); 34-74076 (January 15, 2014), 80 Fed. Reg. 3,674 (January 23, 2015) (SR-

improved transparency for investors and the public on how the exchanges operate. And, also at my request, the SIPs have implemented a time stamp in their data feeds, to facilitate greater transparency on the issue of data latency.<sup>50</sup> In this regard, it should also be noted that the SIPs have steadily upgraded their systems to reduce average latencies from nearly one second a decade ago to less than 1/1000th of a second today.<sup>51</sup>

Another important component of this effort is ensuring that the moderators put in place in 2012 to address extraordinary volatility in the market work well. And the SEC and the SROs are actively reviewing the operation of the limit up-limit down pilot plan, with a focus on issues that occurred during the volatile trading of August 24, 2015.<sup>52</sup> This review has included extensive public analysis by SEC staff of that day's events and the consideration of specific improvements to refine the plan's operation.<sup>53</sup>

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EDGA-2015-02); 34-74072 (January 15, 2015), 80 Fed. Reg. 3,282 (January 22, 2015) (SR-EDGX-2015-02); 34-74357 (February 24, 2015), 80 Fed. Reg. 11252 (March 2, 2015) (SR-CHX-2015-01); 34-74410 (March 2, 2015), 80 Fed. Reg. 12,240 (March 6, 2015) (SR-NYSE-2015-09); 34-74409 (March 2, 2015), 80 Fed. Reg. 12,221 (March 6, 2015) (SR-NYSEArca-2015-11); 74408 (March 2, 2015), 80 Fed. Reg. 12,225 (March 6, 2015) (SR-NYSEMKT-2015-11); and 34-74690 (April 9, 2015), 80 Fed. Reg. 20282 (April 15, 2015) (SR-NASDAQ-2015-033).

<sup>50</sup> See Release No. 34-75505, *Joint Industry Plan: Order Approving Amendment No. 35 to the Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination of Quotation and Transaction Information for Nasdaq-Listed Securities Traded on Exchanges on an Unlisted Trading Privileges Basis Submitted by the BATS Exchange, Inc., BATS Y-Exchange, Inc., Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., International Securities Exchange LLC, NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, Nasdaq Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc.* (July 22, 2015), available at <https://www.sec.gov/rules/sro/nms/2015/34-75505.pdf>; and Release No. 34-75505, *Order Approving the Twenty Second Substantive Amendment to the Second Restatement of the CTA Plan and Sixteenth Substantive Amendment to the Restated CQ Plan* (July 22, 2015), available at <https://www.sec.gov/rules/sro/nms/2015/34-75504.pdf>.

<sup>51</sup> See, e.g., Release No. 34-70010, *Notice of Filing and Immediate Effectiveness of the Nineteenth Charges Amendment to the Second Restatement of the CTA Plan and Eleventh Charges Amendment to the Restated CQ Plan* (July 19, 2013), available at <https://www.sec.gov/rules/sro/nms/nmsarchive/nms2013.shtml>.

<sup>52</sup> See Release No. 34-77679, *Order Approving the Tenth Amendment to the National Market System Plan to Address Extraordinary Market Volatility by Bats BZX Exchange, Inc., Bats BYX Exchange, Inc., Chicago Stock Exchange, Inc., Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ BX, Inc., NASDAQ PHLX LLC, The Nasdaq Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc.* (April 21, 2016), available at <https://www.sec.gov/rules/sro/nms/2016/34-77205.pdf>. See also Testimony of Stephen Luparello, Director, Division of Trading and Markets, SEC, before the United States Senate Committee on Banking, Housing, and Urban Affairs Subcommittee on Securities, Insurance, and Investment (March 3, 2016), available at <https://www.sec.gov/news/testimony/testimony-regulatory-reforms-to-improve-equity-market-structure.html>.

<sup>53</sup> See Research Note: *Equity Market Volatility on August 24, 2015* (December 2015), available at [https://www.sec.gov/marketsstructure/research/equity\\_market\\_volatility.pdf](https://www.sec.gov/marketsstructure/research/equity_market_volatility.pdf).

*Implementing Targeted Initiatives to Optimize Equity Market Structure*

The Commission is also taking action to address enhanced equity market transparency and disclosure, including our proposal issued in November 2015 to update disclosures by alternative trading systems (ATSs),<sup>54</sup> and I expect a proposal imminently to modernize Rules 605 and 606 of Regulation NMS. Updating Rules 605 and 606 could provide investors with important new information about broker-dealer order handling practices, empowering them to better assess the routing decisions of broker-dealers.

The Commission's proposal on Regulation ATS, issued last November, would require ATS platforms that trade national market system (NMS) stocks to provide significant new transparency with respect to their operations. In the years since Regulation ATS was first adopted in 1998, our equity markets have undergone significant change. ATSs are now an important component of our current market structure, fueled by advancements in technology and competing directly with exchanges. Consequently, the number of trading centers has increased substantially, trading activity in NMS stocks is less concentrated, and ATSs collectively now account for approximately 15% of the dollar volume in NMS stocks. This proposal, marking the first-ever major update of Regulation ATS, would require new detailed disclosures about the operation of these platforms and would create a new process for Commission oversight of them.

In addition to enhancing the transparency of our market for investors, the Commission has also advanced measures to improve our core regulatory tools of registration and firm oversight. In March 2015, for example, the Commission proposed important amendments to Rule 15b9-1 to require broker-dealers that engage in off-exchange proprietary trading to become members of a national securities association, which would enhance oversight of active proprietary trading firms.<sup>55</sup> The staff also continues to make progress on recommendations to the Commission to address, among other things, the registration status of certain active proprietary traders, improvements to firms' risk management of trading algorithms, and an anti-disruptive trading rule that would address the use of aggressive, destabilizing trading strategies in vulnerable market conditions.<sup>56</sup>

*Assessing Further Data-Driven Enhancements to Equity Market Structure*

The Commission's continuing work in market structure is a substantial undertaking that requires updates in technology, and utilization of data and analytics to make informed decisions on enhancing market structure. That means new ways of using existing market data through tools like the Market Information Data Analytics System (MIDAS),<sup>57</sup> and it also means building

<sup>54</sup> See Release No. 34-76474, *Regulation of NMS Stock Alternative Trading Systems* (November 18, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-76474.pdf>.

<sup>55</sup> See Release No. 34-74581, *Exemption for Certain Exchange Members* (March 25, 2015), available at <https://www.sec.gov/rules/proposed/2015/34-74581.pdf>.

<sup>56</sup> See Chair White Market Structure Framework Speech, *supra* note 43.

<sup>57</sup> Information regarding MIDAS may be found at <https://www.sec.gov/marketstructure/midas.html>.

new systems to provide even more powerful analytical capabilities for the Commission and our fellow regulators. This past April, the Commission published for comment a proposed national market system plan for the creation of a consolidated audit trail.<sup>58</sup> This is a substantial undertaking and will result in one of the most sophisticated financial databases, providing a full lifecycle of all orders and transactions in our equity and options markets. Final implementation of the consolidated audit trail is a top priority, and I expect the staff to prepare a recommendation for approval of a final plan for Commission action later this year, consistent with Commission Rule 608 under Regulation NMS. After final approval of a plan, Commission Rule 613 requires the selection of a plan processor within two months of approval to build, operate and maintain the consolidated audit trail. Data would be reported by the exchanges and FINRA within one year of Commission approval.

In early 2015, as part of our broader market structure work, the Commission established the Equity Market Structure Advisory Committee to provide a formal mechanism through which the Commission can receive advice and recommendations on key equity market structure issues from a diverse group of experts.<sup>59</sup> The Committee as a whole has since met four times to consider issues such as the operation of Regulation NMS, the impact of access fees and rebates widely used by stock exchanges and the regulatory structure of trading venues, and the impact of various market structure issues on customers. The Committee has established subcommittees to look more closely at specific issues identified by the SEC staff and Committee members before presenting them to the full Committee for discussion and deliberation. The Committee is expected to convene a telephonic meeting on July 8 to receive finalized recommendations from their subcommittees on an access fee pilot program, NMS plan governance, and SRO proposals requiring technology changes. The staff and the Committee will continue to use a variety of tools to ensure both the transparency of the Committee's consideration of issues and input from the full range of investors and other interested market participants, including coordination with our Investor Advisory Committee.

#### *Deepening Oversight of the Fixed Income Markets*

Fixed income market structure has long been a focus at the Commission, and the continued impact of technology, regulation, and other forces require us to deepen our oversight. In particular, as I have remarked before, technology in the fixed income markets may not be

<sup>58</sup> See Release No. 34-77724, *Joint Industry Plan; Notice of Filing of the National Market System Plan Governing the Consolidated Audit Trail* by BATS Exchange, Inc., BATS-Y Exchange, Inc., BOX Options Exchange LLC, C2 Options Exchange, Incorporated, Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., International Securities Exchange, LLC, ISE Gemini, LLC, Miami International Securities Exchange LLC, NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, The NASDAQ Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc. (April 27, 2016), available at <https://www.sec.gov/rules/sro/nms/2016/34-77724.pdf>.

<sup>59</sup> Information regarding the committee and its ongoing work can be found at <https://www.sec.gov/spotlight/equity-market-structure-advisory-committee.shtml>. See also Chair Mary Jo White, *Optimizing our Equity Market Structure: Opening Remarks at the Inaugural Meeting of the Equity Market Structure Advisory Committee* (May 13, 2015), available at <https://www.sec.gov/news/statement/optimizing-our-equity-market-structure.html>.

deployed today to achieve all of the benefits it could for investors, including the broad availability of pre-trade pricing information, lower search costs, and greater price competition.<sup>60</sup>

One important step is to ensure that the best execution and pricing disclosure rules for the corporate bond and municipal securities markets are robust and useful to investors, and FINRA and the MSRB have been moving forward on such reforms. At the Commission's urging,<sup>61</sup> the MSRB in December 2014 adopted a best execution rule for the municipal bond market similar to FINRA's best execution rule.<sup>62</sup> And both SROs have since developed and published additional guidance on the best execution obligations of broker-dealers and municipal securities dealers.<sup>63</sup> In 2014, I also urged both FINRA and the MSRB to move forward on markup and markdown disclosure rules, a reform also publicly supported by my fellow Commissioners.<sup>64</sup> Both have advanced proposals and SEC staff has been dedicated to working closely with FINRA and MSRB as the proposals are finalized.

A related effort in these markets is enhancing pre-trade price transparency. Work on this initiative is underway at the SEC. Pre-trade transparency for corporate bonds and municipal securities should remain a critical objective, and the Commission staff continues to work through the challenging issues inherent in such a transformative market structure change. The staff's immediate goal is to develop a recommendation for the Commission's consideration.

The initiatives in these markets also include interagency work on the U.S. Treasury market in the wake of the events of October 15, 2014.<sup>65</sup> One important priority for the Treasury

<sup>60</sup> See Chair Mary Jo White, *Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors* (June 20, 2014) ("Chair White Fixed Income Speech"), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370542122012>.

<sup>61</sup> See SEC Report on the Municipal Securities Markets (July 31, 2012), available at <http://www.sec.gov/news/studies/2012/munireport073112.pdf>.

<sup>62</sup> See MSRB Rule G-18 (Best Execution); Release No. 34-73764, *Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of a Proposed Rule Change Consisting of Rule G-18, on Best Execution of Transactions in Municipal Securities, and Amendments to Rule G-48, on Transactions with Sophisticated Municipal Market Professionals ("SMMP"), and Rule D-15, on the Definition of SMMP* (December 5, 2014), available at <https://www.sec.gov/rules/sro/msrb/2014/34-73764.pdf>.

<sup>63</sup> See MSRB Implementation Guidance on MSRB Rule G-18, on Best Execution (November 2015), available at <http://www.msrb.org/-/media/Files/MISC/Best-Ex-Implementation-Guidance.ashx?la=en>; and FINRA Regulatory Notice 15-46 (November 2015), available at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Notice\\_Regulatory\\_15-46.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_15-46.pdf).

<sup>64</sup> See, e.g. Chair White Fixed Income Speech, *supra* note 60; and Commissioners Kara M. Stein and Michael S. Piwowar, *Statement on Edward D. Jones Enforcement Action* (August 13, 2015), available at <http://www.sec.gov/news/statement/statement-on-edward-jones-enforcement-action.html>.

<sup>65</sup> See Joint Staff Report: *The U.S. Treasury Market on October 15, 2014* (July 13, 2015), available at [https://www.treasury.gov/press-center/press-releases/Documents/Joint\\_Staff\\_Report\\_Treasury\\_10-15-2015.pdf](https://www.treasury.gov/press-center/press-releases/Documents/Joint_Staff_Report_Treasury_10-15-2015.pdf); Department of Treasury, *Notice Seeking Public Comment on the Evolution of the Treasury Market* (January 22, 2016), available at <https://www.treasury.gov/press-center/press-releases/Documents/Market%20Structure%20RFP%20Final.pdf>.

market is developing a mechanism for post-trade transparency, which systems operated by FINRA and the MSRB already provide in the corporate and municipal markets. Last month, the SEC and Treasury announced the consideration of concrete steps to further enhance post-trade transparency to regulators of the U.S. Treasury cash market, and I look forward to further advancing this effort.<sup>66</sup>

#### *Strengthening Other Critical Market Infrastructures*

Clearing agencies provide vital services to both the equity and fixed income markets every day, and it is vital that the clearance and settlement cycle continue to work effectively and efficiently as the markets grow in size and complexity. The Commission has proposed new rules to enhance the oversight of clearing agencies that are deemed to be systemically important or that are involved in complex transactions, such as security-based swaps.<sup>67</sup> Completing these rules is a priority this year in order to guard against systemic risk that can arise in the clearance and settlement system, and provide certainty to market participants, especially those engaged in cross-border activities. I have also directed the staff to develop a recommendation for the Commission's consideration to shorten the settlement cycle,<sup>68</sup> which should yield a number of benefits including reduced counterparty risk and decreased clearing capital requirements. My fellow Commissioners have expressed strong support for this effort,<sup>69</sup> and it is an important measure for the Commission to advance in coordination with the broader SRO and industry efforts underway.

Last year, again with broad support from all of the Commissioners,<sup>70</sup> the SEC also took the first major step in the regulation of transfer agents in decades, issuing an advance notice of proposed rulemaking, concept release, and request for comment on the full regulatory regime.<sup>71</sup>

<sup>66</sup> See *Statement on Trade Reporting in the Treasury Market* (May 16, 2016), available at <https://www.sec.gov/news/pressrelease/2016-90.html>.

<sup>67</sup> See Release No. 34-71699, *Standards for Covered Clearing Agencies* (March 12, 2014), available at <https://www.sec.gov/rules/proposed/2014/34-71699.pdf>.

<sup>68</sup> See Letter from Chair White to the Investment Company Institute and the Securities Industry and Financial Markets Association (September 16, 2015), available at <https://www.sec.gov/divisions/marketreg/chair-white-letter-to-sifma-ici-2.pdf>.

<sup>69</sup> Commissioners Michael S. Piwowar and Kara M. Stein, *Statement Regarding Proposals to Shorten the Trade Settlement Cycle*, (June 29, 2015), available at <https://www.sec.gov/news/statement/statement-on-proposals-to-shorten-the-trade-settlement-cycle.html>.

<sup>70</sup> See, e.g., Chair Mary Jo White, *Beyond Disclosure at the SEC in 2016* (Feb. 19, 2016), available at <http://www.sec.gov/news/speech/white-speech-beyond-disclosure-at-the-sec-in-2016-021916.html>. See also Commissioners Michael Piwowar and Kara Stein Statement of Support for the Need to Modernize the Commission's Transfer Agent Rules (June 11, 2015), available at <http://www.sec.gov/news/statement/statement-of-support-modernize-sec-transfer-agent-rules.html>.

<sup>71</sup> See Release No. 34-76743, *Transfer Agent Regulations* (December 22, 2015), available at <https://www.sec.gov/rules/concept/2015/34-76743.pdf>.

It is important that this work progress so that the integral work of these market participants continues to serve investors and issuers.

#### **Making Disclosure More Effective for Investors and Issuers**

Another important ongoing initiative is our review of the effectiveness of disclosure for investors and issuers. Following the issuance of the Regulation S-K study required by the JOBS Act,<sup>72</sup> I directed the staff to review comprehensively our disclosure regime for corporate issuers and develop specific recommendations for updating the requirements.<sup>73</sup> The goal is for the staff to make recommendations on how to update our rules to facilitate timely, material disclosure by companies, as well as improving shareholders' access to that information.

This is a comprehensive undertaking and the staff is reviewing the disclosure requirements in phases. In the first phase of the review, the staff is focusing on the business and financial disclosures required by periodic and current reports, Forms 10-K, 10-Q and 8-K, and updates to certain Industry Guides, including Guides 3 and 7. The staff is also considering whether disclosure requirements should be scaled for certain categories of issuers, such as smaller reporting companies or emerging growth companies, and, if so, how. In September 2015, the Commission issued a request for comment for certain financial reporting and disclosure requirements in Regulation S-X.<sup>74</sup>

Most recently, in April 2016, the Commission issued a major concept release that seeks input on modernizing certain business and financial disclosure requirements in Regulation S-K for the benefit of investors and companies.<sup>75</sup> We have already received a number of helpful

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<sup>72</sup> See *Report on Review of Disclosure Requirements in Regulation S-K* (December 2013), available at <https://www.sec.gov/news/studies/2013/reg-sk-disclosure-requirements-review.pdf>.

<sup>73</sup> See Chair Mary Jo White, *The Path Forward on Disclosure* (October 14, 2013), available at <https://www.sec.gov/News/Speech/Detail/Speech/1370539878806>; and Chair Mary Jo White, *The SEC in 2014* (January 27, 2014), available at <https://www.sec.gov/News/Speech/Detail/Speech/1370540677500>.

<sup>74</sup> See Release No. 33-9929, *Request for Comment on the Effectiveness of Financial Disclosures about Entities other than the Registrant* (September 25, 2015), available at <https://www.sec.gov/rules/other/2015/33-9929.pdf>. Regulation S-X contains disclosure requirements that dictate the form and content of financial statements to be included in filings with the Commission. It addresses both registrant financial statements and financial statements of certain entities other than the registrant. It also requires that domestic issuer financial statements filed with the Commission be prepared in accordance with generally accepted accounting principles.

<sup>75</sup> See Release No. 33-10064, *Business and Financial Disclosure Required by Regulation S-K* (April 13, 2016) ("S-K Concept Release"), available at <https://www.sec.gov/rules/concept/2016/33-10064.pdf>. Regulation S-K is the central repository for the Commission's non-financial disclosure requirements. It is intended to foster uniform and integrated disclosure for registration statements under the Securities Act, registration statements under the Securities Exchange Act, and periodic and current reports filed under the Exchange Act. In July 2015, the Commission issued a concept release about possible revisions to audit committee disclosures. See Release No. 33-9862, *Possible Revisions to Audit Committee Disclosures* (July 1, 2015), available at <https://www.sec.gov/rules/concept/2015/33-9862.pdf>.

comment letters on the concept release, which discusses many issues and questions that will also serve as a basis for the study of our disclosure requirements mandated by the FAST Act. In a later phase of the project, the staff will review and consider recommendations regarding the governance and compensation disclosures required in proxy statements.

Importantly, the staff is also considering how companies file their disclosures and is exploring alternatives that could enhance the way that investors access the disclosures. This component of our initiative is of vital importance as technology and investors' needs and behavior evolve. In the near term, we are working on changes to sec.gov that would make EDGAR filings more accessible to investors and easier for them to navigate. We also continue to work to improve the technology behind EDGAR and sec.gov, most recently this week by allowing filers to submit eXtensible Business Reporting Language data inline as part of their core filings to facilitate easier access to, and analysis of, information.<sup>76</sup>

Another important new phase of this ongoing review is to expand it to cover investment companies. Last month, I directed staff in the Division of Investment Management to undertake a disclosure effectiveness initiative of their own to consider ways to improve the form, content, and delivery of funds' disclosures.<sup>77</sup> Staff is in the early stages of prioritizing areas of focus, but I expect they will include ways to leverage advances in technology to improve the presentation and delivery of disclosures and ways to enhance disclosure about fund strategies, investments, risks, and fees.

#### **Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry**

We have also already made significant progress on the Commission's major undertaking to enhance risk monitoring and regulatory safeguards for the asset management industry, which I announced in December 2014.<sup>78</sup> This effort, which comprises five core initiatives addressing funds' evolving portfolio composition risks and operational risks, follows the fundamental reforms to money market funds proposed and adopted during my tenure, which will come fully into effect this October.<sup>79</sup>

<sup>76</sup> See Release No. 34-78041, *Order Granting Limited and Conditional Exemption Under Section 36(a) of the Securities Exchange Act of 1934 from Compliance with Interactive Data File Exhibit Requirement in Forms 6-K, 8-K, 10-Q, 10-K, 20-F and 40-F to Facilitate Inline Filing of Tagged Financial Data* (June 13, 2016), available at <http://www.sec.gov/rules/exorders/2016/34-78041.pdf>.

<sup>77</sup> See Chair Mary Jo White, *The Future of Investment Company Regulation* (May 20, 2016), available at <https://www.sec.gov/news/speech/white-speech-keynote-address-ici-052016.html>.

<sup>78</sup> See Chair Mary Jo White, *Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry* (December 11, 2014), available at <https://www.sec.gov/News/Speech/Detail/Speech/1370543677722>.

<sup>79</sup> See Release No. IC-31166, *Money Market Fund Reform: Amendments to Form PF* (July 23, 2014), available at <https://www.sec.gov/rules/final/2014/33-9616.pdf>.

The Commission has now proposed rules to implement three of the five initiatives I announced in late 2014, all of which I expect will be finalized this year. First, in May 2015, the Commission proposed new rules and forms as well as amendments to its rules and forms to modernize the reporting and disclosure of information by registered investment companies.<sup>80</sup> These proposed rules, if adopted, would require registered funds to provide portfolio-wide and position-level holdings data to the Commission on a monthly basis, as well as report annually on certain census-type information that reflects current information needs. This data would be reported in a structured data format, which would improve the ability of the Commission and the public both to aggregate and analyze information across all funds and to link the reported information with information from other sources. Also in May 2015, the Commission proposed amendments to Form ADV, the primary investment adviser reporting and disclosure form, that would among other things: (1) provide additional information regarding advisers, including information about their separately managed account business; and (2) address issues that staff has identified since the Commission made significant changes to Form ADV in 2011.<sup>81</sup>

To advance the second initiative on liquidity management, in September 2015, the Commission proposed a new rule that would require mutual funds and other open-end investment companies, including ETFs, to adopt and implement liquidity management programs.<sup>82</sup> These funds would also be required to provide enhanced disclosure regarding their liquidity and redemption practices, the methods used by funds to meet redemptions, their committed lines of credit, and interfund borrowing and lending. In addition, mutual funds (except money market funds or ETFs) would be permitted to use “swing pricing,”<sup>83</sup> which would also require additional disclosures.

In December 2015, the Commission advanced the third initiative by proposing a rule that would impose new requirements on the use of derivatives by open and closed-end funds and business development companies.<sup>84</sup> Funds would be required to comply with one of two

<sup>80</sup> See Release Nos. 33-9776; 34-75002; IC-31610, *Investment Company Reporting Modernization* (May 20, 2015), available at <https://www.sec.gov/rules/proposed/2015/33-9776.pdf>.

<sup>81</sup> See Release No. 1A-4091, *Amendments to Form ADV and Investment Advisers Act Rules* (May 20, 2015), available at <https://www.sec.gov/rules/proposed/2015/1a-4091.pdf>. For example, the proposals would, if adopted, require aggregate information related to assets held and use of borrowings and derivatives in separately managed accounts and provide additional information about an adviser's advisory business, including branch office operations and the use of social media.

<sup>82</sup> See Release No. IC-31835, *Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release*, (September 22, 2015), available at <https://www.sec.gov/rules/proposed/2015/33-9922.pdf>.

<sup>83</sup> Swing pricing is the process of reflecting in a fund's net asset value the costs associated with the trading activity of the fund occasioned by shareholders' redemptions and purchases in order to reflect those costs in the prices paid and received by purchasing and redeeming shareholders.

<sup>84</sup> See Release No. IC-31933, *Use of Derivatives by Registered Investment Companies and Business Development Companies* (December 11, 2015), available at <https://www.sec.gov/rules/proposed/2015/ic-31933.pdf>.

alternative portfolio limitations designed to limit the amount of leverage that a fund may obtain through derivatives and certain other transactions. In addition, funds would be subject to asset segregation requirements to manage risks associated with derivatives transactions, as well as requirements to establish risk management programs for their derivatives activities.

The SEC staff is working on recommendations to address the two remaining initiatives that I outlined in 2014: transition planning and stress testing. The former, on which I expect a rule proposal to soon be issued soon, would require investment advisers registered with the Commission to create and maintain transition plans to prepare for a major disruption in their business. Staff is also developing a recommendation that the Commission propose new requirements for stress testing by large investment advisers and large investment companies. Such rules would implement, in part, requirements under section 165(i) of the Dodd Frank Act.

Finally, to further promote compliance with our rules in the asset management space, I have asked the staff to prepare a recommendation to the Commission for proposed rules requiring independent compliance assessments for registered investment advisers. The assessments would not replace examinations conducted by OCIE, but would be designed to improve overall compliance by registered investment advisers.

#### **Advancing Personalized Investment Advice Standard of Conduct**

Section 913 of the Dodd-Frank Act granted the Commission authority to adopt rules to establish a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. As I have stated previously, my evaluation of the differences in the standards that apply to advice under the federal securities laws has led me to conclude that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct when providing personalized investment advice about securities to retail investors. I recognize that this is a complex issue, and that there are significant challenges that will need to be addressed in proposing a uniform fiduciary standard, including how to define the standard, how it would affect current business practices, and the nature of the potential effects on investors, particularly retail investors.

SEC staff has developed a framework for this rulemaking that has been provided to the Commission for its consideration. As part of its analysis in developing its recommendations, the staff is considering, among other things, the SEC staff's 2011 study under Section 913 of the Dodd-Frank Act,<sup>85</sup> the response to the request for information from March 2013,<sup>86</sup> the additional views of investors and other interested market participants, and the potential economic and market impacts. Ultimately, of course, the Commission as a whole will decide whether to

<sup>85</sup> See *Study on Investment Advisers and Broker-Dealers* (January 2011), available at <https://www.sec.gov/news/studies/2011/913studyfinal.pdf>.

<sup>86</sup> See Release Nos. 34-69013 and IA-3558, *Duties of Brokers, Dealers, and Investment Advisers* (March 1, 2013), available at <https://www.sec.gov/rules/other/2013/34-69013.pdf>.

proceed with a rulemaking to implement a uniform fiduciary standard and its parameters. And I will continue to discuss all aspects of this issue with my fellow Commissioners as we proceed.

### Prioritizing Cybersecurity

Cybersecurity is – as I have said before<sup>87</sup> – one of the greatest risks facing the financial services industry and will be for the foreseeable future. Cybersecurity risks can have far-reaching impacts, and robust and responsible safeguards for market participants and investors' information must be maintained. The Commission has been proactive in publicly prioritizing awareness of cyber risks and in examining and enforcing the rules we oversee that relate to cybersecurity.<sup>88</sup>

Our own regulatory efforts are focused primarily on ensuring that our registered entities have policies and procedures to address the risks posed to their systems and data by cyberattacks. In the asset management space, staff from the Division of Investment Management issued guidance that discussed a number of measures that funds and advisers should consider.<sup>89</sup> We are also keeping close watch on how public companies are addressing the issue in accordance with the 2011 guidance issued by the Division of Corporation Finance.<sup>90</sup>

On the exam front, the staff is building on its successful “cybersweep” from last year, and will focus on cybersecurity compliance and controls in 2016 as well.<sup>91</sup> This year's efforts will involve more testing to assess firms' preparedness and implementation of firms' procedures and controls. Also, this past November marked the compliance date for most entities covered by Regulation SCI, which, as noted above, covers certain key market participants – including exchanges, large ATSS, clearing agencies, and others.<sup>92</sup> In particular, Regulation SCI requires those entities to have comprehensive policies and procedures in place surrounding their technological systems to make them more resilient. It also requires those entities to report disruptions in their technology systems to the SEC promptly. The first set of exams of SCI entities with respect to these requirements is underway.

<sup>87</sup> See, e.g., Chair Mary Jo White, *Opening Statement at SEC Roundtable on Cybersecurity* (March 26, 2014), available at <https://www.sec.gov/News/PublicStmnt/Detail/PublicStmnt/1370541286468>.

<sup>88</sup> General information about these activities can be found at <https://www.sec.gov/spotlight/cybersecurity.shtml>.

<sup>89</sup> See *Cybersecurity Guidance*, Investment Management Guidance Update No. 2015-02 (Apr. 2015), available at <https://www.sec.gov/investment/im-guidance-2015-02.pdf>.

<sup>90</sup> CF Disclosure Guidance: Topic No. 2, *Cybersecurity* (October 13, 2011), available at <https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm>.

<sup>91</sup> See also National Exam Program, Risk Alert: Vol. IV, Issue 8, *OCIE's 2015 Cybersecurity Examination Initiative* (Sep. 15, 2015), available at <https://www.sec.gov/ocie/announcement/ocie-2015-cybersecurity-examination-initiative.pdf>.

<sup>92</sup> See SCI Adopting Release, *supra* note 44.

Finally, just last month I added a Senior Advisor for Cybersecurity Policy to my staff, who has deep expertise in cybersecurity and will continue to enhance our coordinated approach to cybersecurity policy across the SEC and engage at the highest levels with market participants and other agencies. While all disruptions from cybersecurity events cannot be prevented, we continue to explore ways to ensure that our regulated entities consider the full range of cybersecurity risks to their businesses and consider and use appropriate tools and procedures to prevent breaches, detect attacks, and limit harm.

#### **Strengthening Compliance with Risk-Based Examinations**

As I know the Committee appreciates, the Office of Compliance Inspections and Examinations (OCIE) plays a critical role in protecting investors and the integrity of our capital markets. OCIE examiners focus on conducting risk-based examinations of registered entities, including broker-dealers, investment advisers, investment companies, national securities exchanges, SROs, transfer agents, and clearing agencies to evaluate their compliance with applicable regulatory requirements. This work is essential to address deficiencies directly with registrants and, more broadly, to improve industry compliance, detect and prevent fraud, inform policy, and identify risks.

Since the September 2014 hearing, OCIE has continued to bolster its risk-based approach by using data analytics to identify activities that may warrant examination as well as deploying technology to make examinations more efficient and targeted. OCIE's Quantitative Analytics Unit has, for example, developed and continues to improve a National Exam Analytic Tool, which allows examiners to analyze huge amounts of trading data in minutes. These efforts and others have enhanced our ability to reach more registrants, and more effectively use our limited examination resources. In FY 2015, OCIE conducted nearly 2,000 formal examinations of registrants, an increase over each of the prior five fiscal years.

In furtherance of its risk-based approach, OCIE publishes its annual public statement of examination priorities to inform investors and registrants about areas that the staff believes present heightened risk. The examination priorities are selected through a collaborative process in which OCIE's senior management and senior representatives of other SEC Divisions and Offices worked side-by-side to analyze and perform a risk-based assessment of information from a number of sources. In 2016, OCIE's stated priorities include ETFs, fee selection practices at investment advisers and dual registrants, variable annuities, retail retirement issues, clearing agencies, cybersecurity, and Regulation SCI compliance. In March, OCIE created a new Office of Risk and Strategy to consolidate and streamline OCIE's risk assessment, market surveillance, and quantitative analysis teams and provide operational risk management and organizational strategy for OCIE.

Deploying technology and the risk-based approaches as described above is imperative and helpful, but they do not and cannot produce sufficient exam coverage. I remain concerned, as I was in September 2014, that we do not have the resources to adequately examine the vast and growing registered investment adviser population, of which there are more than 12,000. The Commission has therefore taken additional steps to prioritize our limited examination resources to better cover investment advisers. In fiscal year 2015, OCIE conducted more than 1,200 examinations of investment advisers, more examinations than any of the previous five years.

OCIE has also made significant enhancements to its examination program for advisers, including hiring additional industry experts, strengthening its examiner training program and increasing its use of advanced quantitative techniques. However, despite these efforts and in light of rapid growth in the adviser population, OCIE was only able to examine approximately 10% of advisers in fiscal year 2015, representing 30% of assets under management.

This level of coverage cannot be allowed to persist. After exploring a number of additional measures, OCIE is now beginning to transition some resources from its broker-dealer examination program to its program for investment advisers and investment companies. Significantly more resources will still be needed to fulfil our responsibility to investors.

#### **Investing in People and Technology for a Smarter, Stronger Commission**

Since I last appeared before this Committee, the Commission has worked hard to enhance its internal operations. The investing public depends on the staff of the Commission and our public systems each day to navigate the securities markets, and it is important that we continue to work to improve the quality of both. For example, we have made increasing investments in information security to improve risk management and monitoring and modernize and secure the SEC's infrastructure. The agency is also engaged in an ongoing, multi-year effort to simplify and optimize the financial reporting process through EDGAR to promote automation and reduce filer burden. With a more modern EDGAR, both the investing public and SEC staff will benefit from having improved access to better data. The steps over the last few years to modernize *SEC.gov* have also continued to improve one of the most widely used federal government websites, making it more flexible, informative, easier to navigate, and secure.

Technology also continues to be the bedrock for much of our ongoing enforcement and examination effort, creating efficiencies and capabilities that were previously impossible. In the last two years, our initiatives have included:

- *Expanding data analytic tools* that assist in the integration and analysis of huge volumes of financial market data, employing algorithms and quantitative models that can lead to earlier detection of fraud or suspicious behavior and ultimately enabling the agency to allocate its resources more effectively. For example, SEC staff has used data analytic (including pattern recognition) tools to, among other things, detect potential fraudulent or manipulative trading, identify financial statement outliers or unusual trends indicative of possible accounting fraud, discover possible money laundering, sift through massive volumes of trading data to detect suspicious trading patterns, and flag higher risk registrants for examination prioritization.
- *Enhancing the Tips, Complaints, and Referral system (TCR)* to bolster its flexibility, configurability, and adaptability. TCR investments will provide more flexible and comprehensive intake, triage, resolution tracking, searching, and reporting functionalities, with full auditing capabilities.

- *Improving enforcement investigation and litigation tracking* to better handle the substantial volume of materials produced during investigations and litigation. Among other initiatives, the SEC needs to build capacity to electronically receive data for tracking and loading (versus the current practice of receiving content via the mail); implement a document management system for Enforcement's internal case files; and revamp the tools used to collect trading data from market participants.

Of course, none of these achievements, including those made possible by enhanced technology, would be possible without the hard work and dedication of the extraordinary women and men who work at the SEC. Our human capital strategy is built to ensure that we continue to attract and retain talented, engaged, and productive employees that reflect the constantly evolving markets we oversee. Since the September 2014 hearing, the Partnership for Public Service named the SEC as the most improved agency in the Best Places to Work in Government annual awards for 2014.<sup>93</sup> And in 2015, the SEC rose to #10 on the Best Places to Work among mid-size agencies list in their annual survey based on the results of our Federal Employee Viewpoint Survey.<sup>94</sup> While these results are encouraging, we remain committed to fostering an even better and stronger workplace to serve the country's investors and its markets.

### Conclusion

The Commission's extensive work to protect investors, preserve market integrity, and promote capital formation goes beyond the initiatives and policies I have discussed. But I have tried by example to convey the breadth and importance of the Commission's ongoing efforts and provide a sense of the agency's work both since my time as Chair and since I last testified before this Committee. While more remains to be achieved, I am very proud of the agency's significant accomplishments across its diverse areas of critical responsibilities. For that, I want to thank first and foremost the exceptional staff of the SEC, as well as my fellow Commissioners, present and past. They richly deserve the praise and confidence of investors and the markets.

In closing, I also want to thank the Chairman, the Ranking Member, and this Committee as a whole for your support of the agency's mission. Your continued support will allow the Commission to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and continue to build upon the significant progress we have achieved.

I am happy to answer any questions that you may have.

<sup>93</sup> See Partnership for Public Service, *The Big Picture: Profiles of Notable Movers*, available at <http://bestplacestowork.org/BPTW/rankings/profiles#sec>.

<sup>94</sup> See Partnership for Public Service, *Best Places to Work Agency Rankings*, available at <http://bestplacestowork.org/BPTW/rankings/overall/mid>.

**RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN SHELBY  
FROM MARY JO WHITE**

**Q.1.** With respect to delegations of authority:

Are all delegations of authority made public? If so, please provide a complete list of all delegations or a Web address where that information can be obtained.

How many delegations of authority are currently in place?

Once the Commission has voted to delegate its authority to staff, how are you and your fellow Commissioners made aware of the staff's use of that authority?

If the Chair is recused on a specific matter, who is accountable for the staff's use of delegated authority?

Are there any formal or informal delegations of authority to staff not directly named in the delegation of authority, and if so, how many? Please provide a specific list of any such formal and informal delegation.

Would you support an SEC review of existing delegations, including an analysis of their appropriateness?

How many SEC staff have the ability by means of delegated authority to issue subpoenas?

**A.1.** In light of the breadth of the Commission's extensive responsibilities, section 4A(a) of the Securities Exchange Act of 1934 (Exchange Act) authorizes the Commission "to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter." The section prohibits the delegation of the function of general rulemaking or the making of any rule pursuant to section 19(c) of the Exchange Act.

The following table provides links to the Commission's delegations of authority that appear in the Code of Federal Regulations:

Person with Delegated Authority	Place Codified	Number of Delegations
Director of the Division of Corporation Finance	17 C.F.R. § 200.30-1 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_61">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_61</a>	55
Director of the Division of Trading and Markets	17 C.F.R. § 200.30-3 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_63">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_63</a>	117
Director of the Office of Municipal Securities	17 C.F.R. § 200.30-3a <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_63a">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_63a</a>	2
Director of the	17 C.F.R. § 200.30-4	17

Division of Enforcement	<a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_64">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_64</a>	
Director of the Division of Investment Management	17 C.F.R. § 200.30-5 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_65">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_65</a>	42
Regional Directors	17 C.F.R. § 200.30-6 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_66">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_66</a>	6
Secretary	17 C.F.R. § 200.30-7 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_67">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_67</a>	14
Hearing Officers	17 C.F.R. § 200.30-9 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_69">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_69</a>	2
Chief Administrative Law Judge	17 C.F.R. § 200.30-10 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_610">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_610</a>	9
Chief Accountant	17 C.F.R. § 200.30-11 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_611">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_611</a>	12
Chief Financial Officer	17 C.F.R. § 200.30-13 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_613">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_613</a>	3
General Counsel	17 C.F.R. § 200.30-14 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_614">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_614</a>	36
Chief Operating Officer	17 C.F.R. § 200.30-15 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_615">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_615</a>	1
Executive Assistant to the Chairman	17 C.F.R. § 200.30-16 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_616">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_616</a>	2
Director of the Office of International Affairs	17 C.F.R. § 200.30-17 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_617">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_617</a>	2
Director of the Office of Compliance Inspections and Examinations	17 C.F.R. § 200.30-18 <a href="http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_618">http://www.ecfr.gov/cgi-bin/text-idx?node=17:3.0.1.1.1&amp;rgn=div5#se17.3.200_130_618</a>	40

In addition, the Commission has delegated to an individual Commissioner, designated as the Commission's "duty officer" by the Chairman from time to time, all of the functions of the Commission, other than general rulemaking or the making of any rule pursuant to section 19(c) of the Exchange Act. 17 CFR §200.43.

To facilitate the performance of delegated functions, section 4B of the Exchange Act authorizes the Chair to assign personnel to perform functions that have been delegated by the Commission to Commission personnel. Specifically, section 4B provides that "there are hereby transferred from the Commission to the Chairman of the Commission the functions of the Commission with respect to the assignment of Commission personnel . . . to perform such functions as may have been delegated by the Commission to the Commission personnel . . . pursuant to section 4A of this title." Under this authority, the Chair has assigned specified staff, under the direction of the person with delegated authority, to perform certain of the functions that have been delegated by the Commission.

Among the delegations of authority, the Commission has delegated to the Director of the Division of Enforcement the authority to designate officers empowered to issue subpoenas in the course of investigations instituted by the Commission pursuant to section 19(c) of the Securities Act of 1933, section 21(b) of the Exchange Act, section 42(b) of the Investment Company Act of 1940, and section 209(b) of the Investment Advisers Act of 1940. The Commission has delegated similar authority to the Director of the Division of Trading and Markets and the General Counsel with respect to investigations instituted pursuant to section 21 of the Exchange Act. Pursuant to section 4B, the Chair has assigned specified persons to perform these delegated functions under the direction of the Director of the Division of Enforcement, the Director of the Division of Trading and Markets, and the General Counsel, as applicable.

The staff is accountable for any exercise of delegated authority through the statutory power of any one Commissioner to request a review of an action taken by delegated authority. Specifically, section 4A(b) of the Exchange Act provides that the Commission retains a discretionary right to review any action taken by delegated authority, upon its own initiative or upon the petition of a party to or intervenor in such action, within such time and in such manner as the Commission by rule shall prescribe. Under the Commission's rules, the Commission may, on its own initiative, order review of any action made by delegated authority at any time, except that where there are one or more parties to the matter, such review shall not be ordered more than 10 days after the action. 17 CFR §201.431(c). The vote of one member of the Commission, conveyed to the Secretary, is sufficient to bring a matter before the Commission for review. In addition, a party to an action made pursuant to delegated authority or a person aggrieved by an action taken by delegated authority may seek Commission review of the action by filing a written notice of intention to petition for review. 17 CFR §201.430.

Given the breadth and scope of the Commission's vast responsibilities, and the need for timely action and responses to market developments, I believe that the framework and subject of staff del-

egations have been appropriately drawn by the Commission. But, as I have previously advised my fellow Commissioners, I am receptive to reconsidering particular delegations of authority that may no longer be appropriate, and to considering whether there are new areas where additional delegations may be appropriate.

**Q.2.** As a follow up to my question at the hearing, please provide specific examples to the following question:

You have often stated that the SEC is an independent agency. While one can expect some split votes because of the way the Commission is set up, there have been many party-line 3–2 and 2–1 votes under your chairmanship. By comparison, according to the press, former Chairman Breeden never had a 3–2 vote, and former Chairman Levitt rarely would take a matter to a vote unless he knew he had a 5–0 vote. Are there any areas that you can work on cooperatively with the other two Commissioners to reach a unanimous decision? Please provide specific examples.

**A.2.** While I believe that it is generally preferable for Commission decisions to be unanimous—and we strive for that—each Commissioner brings his or her unique perspective to matters that come before the agency, and I cannot predict, nor should I dictate, how each member will vote on each matter that comes before the Commission. And, as I indicated at the hearing, a number of our non-unanimous votes during my tenure have occurred on mandated rulemakings to implement certain of the provisions of the Dodd-Frank Act, on which Commissioners continue to have very different views. Nevertheless, during my tenure at the SEC, the Commission has reached unanimous decisions on the majority of matters that have come before it, including on rulemakings.

Most recently, for example, the Commission voted unanimously in August to approve final rules to enhance the information reported by investment advisers and rule amendments to provide authorities with access to data obtained by security-based swap data repositories. The month before, at the Commission’s open meeting on July 13, 2016, the Commission voted unanimously to approve all four rulemakings under consideration, including:

- final rules and guidance under Title VII of the Dodd-Frank Act related to the reporting and dissemination of security-based swap transaction data;
- proposed rules that for the first time would require broker-dealers to disclose specific data regarding order handling information;
- proposed amendments to update certain disclosure provisions by eliminating redundant, overlapping, outdated, or superseded requirements due to changes in rules, accounting principles, and technology; and
- amendments to the Commission’s rules of practice applicable to administrative proceedings.

This year, the Commission also has voted unanimously for, among other things:

- proposed rules for investment adviser business continuity and transition plans;
- final rules requiring security-based swap dealers and major security-based swap participants to provide trade acknowledgments and to verify those trade acknowledgments in security-based swap transactions;
- proposed rules to revise the property disclosure requirements for mining registrants;
- proposed rules to amend the definition of “smaller reporting company” as used in our rules and regulations;
- proposed amendments to address the covered broker-dealer provisions under Title II of the Dodd-Frank Act;
- final rules governing certain security-based swap transactions connected with a non-U.S. person’s dealing activity in the United States;
- final rules for changes to Exchange Act registration requirements to implement Title V and Title VI of the JOBS Act;
- a concept release on business and financial disclosures required by Regulation S-K; and
- interim final rules amending certain issuer disclosure forms (Forms 10-K, S-1, and F-1) and providing for a summary of Form 10-K, to implement provisions of the Fixing America’s Surface Transportation (FAST) Act.

I also note that this is only a partial list—since I have been Chair, there have been many other Commission matters, including the vast majority of votes on initiating or settling enforcement matters, on which the Commission has acted unanimously.

**Q.3.** As a follow up to my question at the hearing, please provide specific examples to the following question:

There have been concerns raised by the public as well as Members of this Committee about repeated violations by SEC registered entities. Two years ago, a former SEC Commissioner stated that, with respect to the most egregious and repeated violations of our securities laws and regulations, “we need to ask ourselves a fundamental question: should the violating entity retain the privilege of participating in our capital markets?” In your opinion, when is it appropriate for the SEC to exercise its ability to deregister an entity? Please provide a specific example of what you would consider to be a valid cause for deregistration.

**A.3.** The SEC has broad authority under the Securities Exchange Act of 1934 (Exchange Act) and Investment Advisers Act of 1940 (Advisers Act) to sanction regulated entities for a variety of misconduct if it finds that the sanction is in the public interest. If a regulated entity engages in misconduct, such as willfully violating, or willfully aiding and abetting a violation of, the securities laws, or is enjoined or convicted of certain specified offenses, the Commission is authorized to pursue a variety of sanctions against that entity. These sanctions include suspending or revoking a regulated entity’s registration. See Section 15(b)(4) of the Exchange Act and

Section 203(e) of the Advisers Act. Revoking a registered entity's registration is the most severe sanction available to the Commission.

The Commission must justify any sanction it imposes by finding that the sanction is necessary to protect the public interest. In determining whether a sanction is in the public interest—including revoking a registered entity's registration—the Commission looks to a broad range of factors. The factors are: (1) the egregiousness of the respondent's actions; (2) whether the violations were isolated or recurrent; (3) the degree of scienter; (4) the sincerity of the respondent's assurances against future violations; (5) the respondent's recognition of the wrongful nature of his or her conduct; and (6) the likelihood that the respondent's occupation will present opportunities for future violations. See *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd* on other grounds, 450 U.S. 91 (1981). The determination is a flexible one and no single factor is controlling. A Commission Order revoking an entity's registration is made in an administrative proceeding in which the entity may contest the allegations made against it and the proposed sanctions. The Commission's determination to revoke an entity's registration is appealable to the Federal appeals courts.

The Commission has revoked the registration of registered entities in cases involving egregious misconduct, such as recurring or systematic violations of the antifraud provisions. For example, the Commission recently issued an opinion revoking an investment adviser's registration and barring its principal for recurring violations of the Advisers Act's antifraud provisions. See *In the Matter of Edgar R. Page and PageOne Financial, Inc.*, Admin. Proc. File No. 3-13037, Advisers Act Release No. 4400 (May 27, 2016), <https://www.sec.gov/litigation/opinions/2016/ia-4400.pdf>. In determining that the revocation of the investment adviser's registration was in the public interest, the Commission noted the egregiousness and recurring nature of the conduct and found that the firm presented a significant risk of future misconduct. See *id.* at 15-17.<sup>1</sup>

**Q.4.** In a speech earlier this year you stated that the SEC is “engaged with our fellow financial and consumer protection regulators, including the Department of Treasury, the Federal Reserve, the CFPB, OCC, FTC, and FDIC, to develop a broader understanding of the online marketplace lending industry, and regulatory initiatives that would enhance investor, consumer and borrower protections.” Please explain what role the SEC has had in developing regulatory initiatives in the online marketplace lending sphere and describe the SEC's future plans in this area.

**A.4.** As in other subject areas, the Commission's role in the area of online marketplace lending is the protection of investors in connection with the offer and sale of securities. Obtaining money from investors to fund borrower loans through an online lending platform involves the offer and sale of securities. The Commission does

<sup>1</sup> See also “*In the Matter of J.S. Oliver Capital Mgmt. L.P., and Ian O. Mausner*, Admin. Proc. File No. 3-15446, Exchange Act Release No. 78098 (June 17, 2016), <https://www.sec.gov/litigation/opinions/2016/33-10100.pdf> (Commission revoked investment adviser's registration and barred its principal where respondents repeatedly violated the antifraud provisions by systematically fraudulently allocating trades and failing to disclose material information to investors).

not oversee the lending activities of online lenders and extensions of credit.

Commission staff has engaged in discussions with other agencies and the Treasury Department to keep apprised of developments in the marketplace and to enhance others' understanding of how the Federal securities laws apply to these activities. I support the continuation of the interagency staff working group to help determine whether regulatory initiatives would be appropriate.

**Q.5.** I have previously raised concerns about the accountability and transparency of the Financial Stability Board (FSB). The FSB is not a U.S. regulator, it is not accountable to Congress or the American people, and yet it issues directives that U.S. regulators often adopt in some form. As the Chair of the SEC, you are a member of the FSB Plenary. Please provide a list of all FSB Plenary meetings and any other FSB meeting that you have been invited to attend or participate in, annotating which ones you attended and/or participated in person, telephonically or not at all. For the last category, please provide the names and titles of SEC staff that participated or attended in your place. If you are unable to attend an FSB meeting in person, have you considered sending another Commissioner, and if not, why not?

**A.5.** The FSB has a number of committees whose meetings I, another Commissioner, or senior SEC staff attend. With the exception of the first meeting after I joined the SEC held in April 2013, I have personally participated in all of the meetings of the FSB Steering Committee, which is the leadership group within the FSB. Prior to my tenure as Chair, Chairman Shapiro had Commissioner Elisse Walter attend such meetings, as she did the April 2013 meeting. In another change from prior practice, I or, at my request, another Commissioner has also personally attended nearly all board meetings of IOSCO. With respect to meetings of the other committees of the FSB, including the Plenary, I have continued the existing practice of having SEC senior staff attend.

Members of the SEC staff attend the FSB Plenary and meetings of the standing committees in which the SEC participates, which are: (i) the Standing Committee on Supervisory and Regulatory Cooperation (SRC); (ii) the Standing Committee on Assessment of Vulnerabilities (SCAV); and (iii) the Standing Committee on Standards Implementation (SCSI).

Currently, meetings of the Plenary and the SRC are attended by Paul Leder (Leder), Director of the Office of International Affairs (OIA), and meetings of the SCAV, which the SEC joined in 2015, are attended by Mark Flannery (Flannery), Director of the Division of Economic and Risk Analysis (DERA). Meetings of the SCSI are attended by Katherine Martin (Martin), Associate Director in the Office of International Affairs.

Below is a list of the FSB Steering Committee, Plenary, and standing committee meetings I, another Commissioner, or an SEC staff member attended during my time as SEC Chair. Meetings where attendance was by phone are noted by an asterisk.

FSB Meetings April 2013 – Present		
Date	Meeting	Participant
<b>2013</b>		
4/20/2013	STEERING COMMITTEE	COMMISSIONER ELISSE WALTER
5/8/2013	SRC*	ROBERT FISHER (“FISHER”), OIA ACTING DIRECTOR
6/10/2013	SRC	FISHER
6/12/2013	SCSI*	ERIC PAN (“PAN”), OIA ASSOCIATE DIRECTOR
6/24/2013	PLENARY	FISHER
7/15/2013	SCSI	PAN
8/6/2013	SRC*	FISHER
8/12/2013	STEERING COMMITTEE*	CHAIR MARY JO WHITE (“WHITE”)
8/20/2013	PLENARY*	ELIZABETH JACOBS, OIA DEPUTY DIRECTOR
10/2-3/2013	SRC	FISHER
10/23/2013	SCSI*	PAN
11/8/2013	PLENARY	FISHER
12/5-6/2013	SCSI	PAN
12/9/2013	SRC*	FISHER
<b>2014</b>		
1/13/2014	STEERING COMMITTEE	WHITE
3/6/2014	SRC	LEDER
3/10/2014	SCSI	PAN AND THOMAS BUTLER, OFFICE OF CREDIT

		RATINGS DIRECTOR
3/31/2014	PLENARY	LEDER
5/22/2014	SCSI*	PAN
6/3/2014	SRC	LEDER
6/23/2014	SCSI*	PAN
6/26/2014	SRC*	LEDER
6/30/2014	STEERING COMMITTEE	WHITE
7/3/2014	SRC*	LEDER
7/31/2014	STEERING COMMITTEE*	WHITE
8/29/2014	SCSI	PAN
9/2/2014	SRC	LEDER
9/17-18/2014	PLENARY	LEDER
10/7/2014	SRC*	LEDER
10/15/2014	SCSI*	PAN
10/28/2014	STEERING COMMITTEE*	WHITE
11/4/2014	PLENARY*	LEDER
12/5-6/2014	SCSI	PAN
<b>2015</b>		
1/11/2015	STEERING COMMITTEE	WHITE
1/15/2015	SCSI*	PAN
1/29/2015	SCSI*	PAN
2/3/2015	SRC	LEDER
3/7/2015	SCAV	FLANNERY
3/10/2015	SCSI	PAN
3/13/2015	STEERING COMMITTEE*	WHITE
3/19/2015	SRC*	LEDER
3/26/2015	PLENARY	LEDER
5/6/2015	SRC*	PAN
5/12-13/2015	SCSI	PAN
5/27/2015	SRC*	LEDER
6/23/2015	SRC	LEDER
6/29/2015	SCAV/SRC	FLANNERY
7/2/2015	SCSI*	PAN
7/17/2015	STEERING COMMITTEE	WHITE
8/31/2015	STEERING COMMITTEE	WHITE
9/7-8/2015	SCAV	FLANNERY
9/7-8/2015	SCSI	PAN
9/17/2015	STEERING COMMITTEE*	WHITE
9/22/2015	SRC*	LEDER
9/25/2015	PLENARY	LEDER
10/15/2015	SRC*	KATHLEEN HUTCHINSON ("HUTCHINSON"), OIA ASSISTANT DIRECTOR
10/15/2015	SCSI*	HUTCHINSON

10/16/2015	SCSI*	HUTCHINSON
10/23/2015	PLENARY*	LEDER
11/18/2015	SRC*	LEDER
11/30/2015- 12/1/2015	SRC	LEDER
12/7/2015	SCSI	LEDER
2016		
1/11/2016	STEERING COMMITTEE*	WHITE
1/28/2016	SCSI*	MARTIN
3/3/2016	SCSI*	MARTIN
3/21/2016	SRC	LEDER
3/29/2016	SCAV	JENNIFER MARIETTA- WESTBERG, DERA DEPUTY DIRECTOR
3/30-31/2016	PLENARY	LEDER
5/23/2016	SRC*	LEDER
5/25/2016	STEERING COMMITTEE	WHITE
5/25/2016	SCSI*	MARTIN
6/20/2016	STEERING COMMITTEE*	WHITE
6/27/2016	SCSI	MARTIN

**Q.6.** A recent news article stated that “passive investing is taking over the money-management world” and as a result, “mutual funds are facing extinction.” Is the SEC studying this issue, and if so, when do you expect the results of that study? If not, what is the SEC doing to permit innovation and competition to thrive in this space? Do you anticipate to have any legislative recommendations for Congress to consider?

**A.6.** The Commission and its staff generally monitor trends within the asset management industry, including those related to mutual funds and exchange-traded funds (ETFs). Recent industry data suggests an increasing trend towards passive investing. While overall investor demand for mutual funds declined in 2015, industry data indicates that demand for both index-based mutual funds and index-based ETFs has increased.<sup>2</sup> The Commission staff generally does not believe that this recent trend toward passive investing—which may or may not continue over the long term—will eliminate the role in the investment company marketplace for mutual funds and ETFs, whether passively or actively managed, as each product line presents its own relative set of advantages and disadvantages to different investor groups.

The Commission’s mission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Consistent with its mission, the Commission continues to evaluate

<sup>2</sup> See generally, Lipperus U.S. Fund Flows, <http://www.lipperusfundflows.com>; Morningstar Direct U.S. Asset Flows Update: Data through Dec. 31, 2015, U.S. Mutual Funds and Exchange-Traded Products (Jan. 15, 2016), <http://corporate.morningstar.com/US/documents/AssetFlows/AssetFlowsJan2016.pdf>; and Investment Company Institute, 2016 Investment Company Factbook 26-30 (2016), [https://www.ici.org/pdf/2016\\_factbook.pdf](https://www.ici.org/pdf/2016_factbook.pdf).

and, as appropriate, approve requests for exemptive relief for new and novel investment products, including ETFs. The Commission evaluates all exemptive application requests to operate such investment products under the standards prescribed by the Investment Company Act of 1940—that is, such exemption must be necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Investment Company Act. The Commission has approved, over the years, a number of exemptive applications under this statutory exemptive authority, including applications submitted by sponsors to operate various types of actively managed ETFs.

I do not anticipate the Commission making legislative recommendations regarding ETFs at this time.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR BROWN  
FROM MARY JO WHITE**

**Q.1.** At the June 14 hearing, you were asked about the legislation introduced in the House of Representatives regarding Business Development Companies (BDCs) and your investor protection concerns with respect to the changes that would increase the leverage used by BDCs. Specifically, you were asked why you are particularly concerned by the increase in leverage for BDCs when investors have access to other investments with leverage, including securities purchased on margin, listed options, or shares of banks that operate on a leveraged basis.

For clarification, please describe any limitations on the purchase of those investments, as well as any limitations on similar instruments such as 3x leveraged exchange traded funds. Please include in your discussion any regulatory requirements or guidance, or stock exchange regulations, such as options or margin account approval, or limitations on margining low-priced or illiquid shares, that broker-dealers must comply with or consider for clients who wish to trade those instruments.

In addition, you mentioned that BDC shares are predominately held by retail investors. Based on the most recent data available, please provide the portion of investors in BDC shares and listed options that are “retail” investors. Also, please provide data, to the extent available, of the percentage of retail investors that have brokerage accounts authorized to use margin. Finally, please discuss any investor protection concerns that might exist in an initial offering of BDC shares aimed at retail investors.

**A.1.** As entities regulated under the Investment Company Act of 1940 (1940 Act), BDCs, as well as other types of funds, such as mutual funds, closed-end funds, and exchange-traded funds (ETFs), are subject to statutory provisions and regulations that are designed to protect investors. There are also various regulatory requirements with which investment advisers and broker-dealers must comply when making a recommendation in connection with a securities transaction or investment strategy involving securities, including those involving investments in BDCs or ETFs and those using options or a margin account.

*Investment Companies.* The 1940 Act was enacted, in part, to provide “small investors” with “a regulated institution for the investment of their savings.”<sup>1</sup> Many of the 1940 Act’s provisions correspond to abuses that contributed to the rapid decline in the value of closed-end investment companies at the end of the 1920s. Section 18 (which is applicable to BDCs), for example, was intended to protect investors from abuses associated with complex capital structures, including excessive leverage.<sup>2</sup>

Congress created BDCs in 1980 as a specialized type of closed-end investment company operated for the purpose of providing capital for small, growing, and financially troubled domestic operating companies. Congress recognized the need to “avoid compromising needed protections for investors in the name of reducing regulatory burdens.”<sup>3</sup> Under the 1940 Act, the regulation of BDCs is the same as the regulation of registered closed-end funds with modifications that generally allow BDCs greater operating flexibility.<sup>4</sup>

From my perspective, increasing leverage for BDCs would give rise to significant investor protection concerns. Section 18 of the 1940 Act requires open-end funds (including mutual funds and ETFs) and closed-end funds to comply with 300 percent asset coverage requirements.<sup>5</sup> In comparison, BDCs must comply with a 200 percent asset coverage requirement for senior securities representing indebtedness (i.e., debt) and senior securities that are stock (i.e., preferred stock).<sup>6</sup>

For example, a BDC with assets worth \$100 and no liabilities can borrow \$100 for \$200 in total assets. If the value of those assets subsequently falls 25 percent, then the BDC holds assets worth \$150 but still owes the lender \$100. Thus, the BDC’s share-

<sup>1</sup> See H.R. Rep. No. 76-2639, at 10 (1940). See also S. Rep. No. 76-1775, at 12 (1940). Because the Act was enacted, in part, to provide “small investors” with “a regulated institution for the investment of their savings,” the 1940 Act includes far more extensive substantive regulation—e.g., prohibitions on transactions between an investment company and its affiliates—than the other Federal securities laws.

<sup>2</sup> The section balances the interests of fund shareholders and the holders of senior securities—e.g., preferred stock or debt securities issued by the fund. Section 1(b) of the 1940 Act states that the national interest is adversely affected “when investment companies by excessive borrowing and the issuance of excessive amounts of senior securities increase unduly the speculative character of their junior securities [i.e., common stock].” 15 U.S.C. §80a-1(b). Section 1(b) further states that the Act is to be interpreted “to mitigate and, so far as is feasible, to eliminate the conditions enumerated in this section which adversely affect the national public interest and the interest of investors.” *Id.*

<sup>3</sup> See H.R. Rep. No. 96-1341, at 22 (1980); S. Rep. No. 96-958, at 5 (1980).

<sup>4</sup> A BDC, for example, may issue more debt securities as a percentage of total assets than other closed-end funds, may issue debt in multiple classes, may issue long-term options and warrants, and is subject to relaxed regulation of transactions with affiliates. See Investment Company Act §§61(a)(1), 61(a)(3), and 57(d), 15 U.S.C. §§80a-60(a)(1), -60(a)(2), -(56)(d).

<sup>5</sup> Open-end funds are prohibited from issuing or selling any “senior security” other than borrowing from a bank and must maintain 300 percent asset coverage after any such borrowing. Investment Company Act §18(f)(1), 15 U.S.C. §80a-18(f)(1). Section 5(a)(1) of the 1940 Act defines “open-end company” as “a management company which is offering for sale or has outstanding any redeemable security of which it is the issuer.” 15 U.S.C. §80a-5(a)(1). Closed-end funds registered under the 1940 Act are also required to have 300 percent asset coverage for debt, but their ability to issue senior securities representing indebtedness is not limited to bank borrowings, and they may issue senior securities that are stock, subject to certain limitations and a more liberal 200 percent asset coverage requirement, with both asset coverage requirements being measured at the time of issuance. Unlike open-end funds, BDCs and closed-end funds are required to maintain the asset coverage at the time of issuance of senior securities and are subject to limits on distributions to holders of the common stock and repurchases of common stock if the asset coverage requirements are not met. Investment Company Act §18(a)(1)(A), 15 U.S.C. §80a-18(a)(1)(A). Section 5(a)(2) of the Investment Company Act defines “closed-end company” as “any management company other than an open-end company.” 15 U.S.C. §80a-5(a)(2).

<sup>6</sup> See Investment Company Act §61(a)(1), 15 U.S.C. §80a-60(a)(1).

holders' equity dropped from \$100 to \$50. Shareholders' equity declined by 50 percent although the value of the BDC's assets declined only 25 percent, and the asset coverage fell from 200 percent to 150 percent.

Reducing the required asset coverage, for example to 150 percent, would permit that same BDC to borrow \$200, effectively doubling its leverage, for \$300 in total assets. If the value of those assets subsequently falls 25 percent, then the BDC holds assets worth \$225 but owes the lender \$200. Thus, the BDC's shareholders' equity dropped from \$100 to \$25. Shareholders' equity declined by 75 percent although the value of the BDC's assets declined by 25 percent, and the asset coverage fell from 150 percent to 112.5 percent.

Increasing BDC leverage increases the potential losses for both holders of BDC common stock and BDC debt and preferred stock. My concern is heightened because BDC common stock is predominantly held by retail investors. Retail investors account for nearly 70 percent of BDC common stock ownership.<sup>7</sup> In addition, retail investors account for an unknown percentage of debt securities issued by BDCs.<sup>8</sup>

Use of leverage in funds continues to be a significant focus for the Commission and staff. In December 2015, the Commission proposed a new rule regarding the use of derivatives by mutual funds, ETFs, closed-end funds, and BDCs.<sup>9</sup> SEC staff is also focusing resources on examinations of ETFs' compliance with applicable regulatory requirements, sales strategies, trading practices, and disclosures, including excessive portfolio concentration, primary and secondary market trading risks, adequacy of risk disclosure, and suitability, particularly in niche or leveraged/inverse ETFs.<sup>10</sup>

*Investment Advisers and Broker-Dealers.* Investment advisers and broker-dealers must comply with various regulatory requirements when making a recommendation in connection with a securities transaction or investment strategy involving securities, includ-

<sup>7</sup>This calculation is an average, weighted by total assets, of 72 active BDCs with securities registered under the Securities Act of 1933. Of this number, 21 are nontraded BDCs, and 51 are traded on securities exchanges or over the counter. Commission staff calculated this average internally using publicly available information on institutional ownership. The institutional ownership percentage for each BDC was subtracted from 100 percent to determine the retail ownership percentage. A recent report on the BDC industry states that the average institutional ownership of 46 exchange traded BDCs is 24.9 percent. This percentage is a simple average of the institutional ownership percentage for each of the 46 BDCs and excludes ownership by brokers and private bank/wealth management firms, as reported in FactSet, a data service. See *BDC Industry Investment Banking Weekly Newsletter* (Raymond James), July 15, 2016.

<sup>8</sup>For example, since 2012, over a dozen BDCs have issued "baby bonds" (i.e., fixed income securities issued in small denominations and traded on a securities exchange) in \$25 denominations. This information is based on Commission staff review of Form N-2 filings by BDCs with the Commission. BDCs register under the Securities Act of 1933 public offerings of their securities on Form N-2.

<sup>9</sup>See "Use of Derivatives by Registered Investment Companies and Business Development Companies", Investment Company Act Release No. 31933, 80 FR 80883 (Dec. 28, 2015), <https://www.sec.gov/rules/proposed/2015/ic-31933.pdf>.

<sup>10</sup>See "Office of Compliance Inspections and Examinations, SEC, Examination Priorities for 2016" (Jan. 11, 2016), <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2016.pdf>. Leveraged ETFs are highly specialized investment vehicles that seek to replicate the performance of an underlying index each day. For example, a 3x ETF is designed to produce a daily return equal to three times the return of a specified index. Thus, a 3x ETF can magnify the amount of an investor's gain or loss. Leveraged ETFs are designed to achieve their stated objectives on a daily basis; they are not designed for buy and hold investors. See "SEC Office of Investor Education and Advocacy and Financial Industry Regulatory Authority, Investor Alert on Leveraged and Inverse ETFs: Specialized Products With Extra Risks for Buy-and-Hold Investors" (Aug. 18, 2009), <https://www.sec.gov/investor/pubs/leveragedetfs-alert.htm>.

ing strategies utilizing derivatives and leverage. For example, investment advisers must make a reasonable determination that the investment advice provided is suitable for the client based on the client's financial situation and investment objectives.<sup>11</sup> Similarly, a broker-dealer recommending particular investments has an obligation to only make suitable securities recommendations to their customers, taking into account the particular circumstances and investment goals of each investor.<sup>12</sup> Heightened suitability obligations, as well as enhanced account opening requirements, apply to listed options.<sup>13</sup> In addition, FINRA guidance reminds members that leveraged ETFs typically are unsuitable for retail investors who plan to hold them for longer than one trading session, particularly in volatile markets,<sup>14</sup> and that members have certain obligations in connection with the sale or recommendation of complex investment products, including derivatives.<sup>15</sup>

Securities margin accounts are also subject to a comprehensive system of regulation.<sup>16</sup> In general, any equity security that is listed on a national securities exchange is margin eligible. However, broker-dealers often have more restrictive house-margin requirements where they may not extend margin on certain securities such as low-priced equities. The Commission staff does not maintain statistics on the number of retail investors with margin accounts. We also understand that not all retail investors who open

<sup>11</sup> See "Status of Investment Advisory Programs under the Investment Company Act of 1940", Investment Company Act Release No. 22579, 62 *FR* 15098 (Mar. 31, 1997), <https://www.sec.gov/rules/final/ic-22579.txt> (citing "Suitability of Investment Advice Provided by Investment Advisers", Investment Advisers Act Release No. 1406, 59 *FR* 13464 (Mar. 22, 1994)).

<sup>12</sup> See, e.g., FINRA, "Regulatory Notice 12-55: Suitability" (Dec. 2012), <http://www.finra.org/sites/default/files/NoticeDocument/p197435.pdf> (providing guidance on FINRA's suitability rule); FINRA, "Regulatory Notice 11-25: Know Your Customer and Suitability" (May 2011), <http://www.finra.org/sites/default/files/NoticeDocument/p123701.pdf> (providing guidance on new FINRA Rule 2111). In addition, there are enhanced suitability and disclosure obligations in connection with penny stock transactions. See Exchange Act Section 15(h), 15 U.S.C. §78o(h) and Exchange Act Rules 3a51-1 and 15g-1 through 15g-100, 17 CFR §§240.3a51-1, .15g-1 to 100. A small number of BDCs disclose that because of their stock price, they are subject to the penny stock rules.

<sup>13</sup> A broker-dealer is also subject to FINRA Rule 2360(b)(16) with respect to its suitability obligations and the opening of an options account. More specifically, FINRA Rule 2360(b)(16) requires its members to exercise due diligence to ascertain the essential facts relative to a customer, his or her financial situation and investment objectives when considering whether to open an account for that customer to trade options. In addition, FINRA Rule 2360(b)(19) subjects its members' recommendations to engage in options trading (including whether to open an account and the subsequent recommendations for that account) to heightened suitability obligations.

<sup>14</sup> See FINRA, "Regulatory Notice 09-31: Non-Traditional ETFs" (June 2009), <http://www.finra.org/sites/default/files/NoticeDocument/p118952.pdf>. See also FINRA, "Regulatory Notice 12-03: Complex Products" (Jan. 2012), <http://www.finra.org/sites/default/files/NoticeDocument/p125397.pdf> (providing guidance to firms about heightened supervision of complex products, including, among others, inverse or leveraged ETFs).

<sup>15</sup> See FINRA, "Regulatory Notice 12-03: Complex Products" (Jan. 2012), <http://www.finra.org/sites/default/files/NoticeDocument/p125397.pdf>. See also NASD, "Notice to Members 03-71: Non-Conventional Investments" (Nov. 2003), <https://www.finra.org/sites/default/files/NoticeDocument/p003070.pdf> (reminding members of their obligations when selling "nonconventional investments," such as asset-backed securities, distressed debt and derivative products).

<sup>16</sup> See, e.g., Federal Reserve's Regulation T, 12 CFR §§220.1 to 220.132; Exchange Act Rule 10b-16, 17 CFR §240.10b-16; FINRA Rules 2360 (Options); FINRA Rule 2264 (Margin Disclosure Statement); FINRA Rule 4210 (Margin Requirements). See also FINRA, "Regulatory Notice 11-15: Low-Priced Equity Securities" (Apr. 2011), <http://www.finra.org/sites/default/files/NoticeDocument/p123431.pdf> (reminding firms to consider risks associated with low-priced equity securities when extending credit in a strategy-based or portfolio margin account); FINRA, "Regulatory Notice 09-53: Non-Traditional ETFs" (Aug. 2009), <http://www.finra.org/sites/default/files/NoticeDocument/p119906.pdf> (outlining increased margin requirements for leveraged ETFs and associated uncovered options).

margin accounts actually purchase shares on margin (e.g., some investors may view such accounts as overdraft protection).

**Q.2.** Please clarify your understanding of the jurisdiction of the Department of Labor (DOL) with respect to retirement accounts that are covered by the Employee Retirement Income Security Act and its related rules and the SEC's jurisdiction over broker-dealers or investment advisers that service those accounts. To the extent it is relevant, please elaborate on the comment you made about how the historic overlap of SEC and DOL jurisdiction has been managed.

**A.2.** The DOL and the SEC are separate agencies with their own perspectives, jurisdiction, and statutory authority. The SEC oversees and enforces the Federal securities laws, including the Exchange Act with respect to broker-dealers and the Investment Advisers Act of 1940 with respect to investment advisers. In general, a "broker" is any person engaged in the business of effecting transactions in securities for the account of others, a "dealer" is any person engaged in the business of buying and selling securities for such person's own account, and an "investment adviser" is any person engaged in the business of advising others regarding securities for compensation.<sup>17</sup>

I am not in a position to describe in detail DOL's jurisdiction under the Employee Retirement Income Security Act of 1974 (ERISA) or the Internal Revenue Code of 1986. In general terms, however, the statutes set minimum standards for employee benefit plans and provide protections to plan participants, including by prescribing certain requirements and responsibilities for fiduciaries of those plans.<sup>18</sup> A "fiduciary" includes a person who exercises discretionary authority or control with respect to the management of a plan or disposition of its assets, renders investment advice for a fee or other direct or indirect compensation, or has any discretionary authority or responsibility in the administration of a plan.<sup>19</sup>

An SEC-regulated broker-dealer or investment adviser that works with accounts governed by these statutes must comply with their requirements in addition to what is demanded of the financial institution under the Federal securities laws. For example, advisory firms that provide advice as fiduciaries under both the ERISA and SEC regulatory regimes must ensure that their practices comply with the provisions for fiduciaries under both regimes, which may include steps to address differences between the two sets of requirements (e.g., different contract provisions for accounts subject to ERISA and accounts not subject to ERISA).

The interplay between the DOL's regulations and the requirements under the Federal securities laws, and the application of different standards to the provision of investment advice to retail investors, are important issues. Consultation among the staff from the DOL and SEC has been important to manage any conflicts and issues that may arise related to the application of our separate regimes and mandates. For example, in 2011 staff from the Division

<sup>17</sup> See Exchange Act §3(a)(4)-(5), 15 U.S.C. §78c(a)(4)-(5); Investment Advisers Act §202(a)(11), 15 U.S.C. §80b-2(a)(11).

<sup>18</sup> See, e.g., 29 U.S.C. §1104 (standard of care for fiduciaries).

<sup>19</sup> See 29 U.S.C. §1002(21) (definition of fiduciary).

of Investment Management issued a letter stating that disclosure to participants and beneficiaries of certain plan and investment-related information required by a rule under ERISA, including performance information, would be treated as satisfying the SEC's rules on mutual fund advertising, notwithstanding differences among the requirements.<sup>20</sup> More recently, SEC staff consulted with DOL staff on the Commission's security-based swap business conduct rulemaking and the intersection of ERISA fiduciary status with the Dodd-Frank Act business continuity provisions.<sup>21</sup> Consultation will continue to be important as the DOL's new conflict of interest rule comes into effect.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR CRAPO  
FROM MARY JO WHITE**

**Q.1.** In a speech at Stanford you highlighted that fintech has “the potential to transform how our markets operate in virtually every respect—from streamlined market operations to more affordable ways to raise capital and advise clients.”

I am interested in the approach the UK has taken to fintech, such as Project Innovate. Do you expect the SEC will explore ways to better understand fintech through roundtables and other outreach efforts?

**A.1.** The staff continues to monitor fintech developments in the securities industry and engage market participants to analyze the potential effect of new technologies on market efficiency, capital formation, and investor protection. This monitoring includes direct outreach to and discussions with industry participants, and staff is considering whether a roundtable or other more formal outreach mechanisms will foster staff's understanding of these issues.

For example, established and new firms have been exploring the application of distributed ledger technology to potentially improve or replace existing processes across the infrastructure of the securities markets. Some of these firms appear to be developing applications that could be implemented in the clearance and settlement of securities. The staff has met with several of these firms to discuss their activity in this setting as well as consider potential regulatory implications. The Commission has also solicited comment on the utility of the new technology. For example, in response to a recent Advanced Notice of Proposed Rulemaking and Concept Release on transfer agent regulations, the Commission received industry feedback on the possible use of distributed ledger technology by transfer agents.

**Q.2.** In response to a question from Senator Toomey on Rule 18f-4 and potential unintended consequences, you suggested that the

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<sup>20</sup> See U.S. Dept. of Labor, SEC No-Action Letter (Oct. 26, 2011), [www.sec.gov/divisions/investment/noaction/2011/dol102611-482.htm](http://www.sec.gov/divisions/investment/noaction/2011/dol102611-482.htm).

<sup>21</sup> Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, Exchange Act Release No. 77617, 81 *FR* 29959, 29965-66 (May 13, 2016), <https://www.sec.gov/rules/final/2016/34-77617.pdf> (clarifying that security-based swap dealers and major security-based swap participants would not be ERISA fiduciaries solely for complying with the Commission's external business conduct rules). See also 29 CFR §2510.3-21(c)(2) (providing that the provision of any advice to an employee benefit plan shall not cause a security-based swap dealer or major security-based swap participant to be deemed to be an ERISA fiduciary, where certain conditions are met).

SEC is reviewing the comment letters and working to improve the rule. I encourage you to consider the merits of the comment letters on how best to account for the actual amount of market risk exposure and work to tailor the rule accordingly.

Can you commit to doing so as part of the rulemaking process?

**A.2.** To date, the Commission has received more than 180 comment letters on proposed Rule 18f-4, and Commissioners and members of the staff collectively have held more than 50 meetings with commenters and other interested parties to discuss the proposal. The staff is currently reviewing the comment letters, and the Commission will carefully consider all of them, including those urging the Commission to consider adjustments to the proposed rule's exposure limitations, as the Commission works to finalize Rule 18f-4.

#### **RESPONSES TO WRITTEN QUESTIONS OF SENATOR KIRK FROM MARY JO WHITE**

**Q.1.** Chair White, the Commission recently updated its interpretative release regarding automated quotations under regulation NMS to allow for delays in price quotations. As part of that release, the Commission announced that it would conduct a study within 2 years regarding the effects of any intentional access delays on market quality, including asset pricing, and report back to the Commission with the results of any recommendations. Based on that study, or earlier, the Commission stated that it will "reassess whether further action is appropriate."

Which office at the Commission will be responsible for conducting the aforementioned study?

What factors will the Commission be monitoring to determine if "further action is appropriate" before the aforementioned study is completed?

What types of problems could arise due to the issuance of the updated interpretative release that could prompt the Commission to reassess its position?

Given that the issue of delayed quotes raises fundamental concerns about the structure and efficiency of our financial markets, why did you decide to approve IEX's application rather than undertake a rulemaking?

**A.1.** In response to technological and market developments since the adoption of Regulation NMS in 2005, as well as novel proposals like IEX's exchange application, the Commission proposed and subsequently adopted an interpretation under Regulation NMS that "immediate" in the context of Regulation NMS does not preclude a de minimis intentional delay—i.e., a delay so short as to not frustrate the purposes of the trade-through rule of Regulation NMS by impairing fair and efficient access to an exchange's quotations. The Commission sought public comment on its proposed update to its prior interpretation of "immediate" in Regulation NMS, publishing a draft for review and comment by investors, broker-dealers, and other interested parties. These comments were carefully reviewed and taken into account in preparing the final interpretation.

The Commission's interpretation referenced a study to be completed by Commission staff within 2 years regarding the potential effects of intentional access delays on market quality, including

price discovery. That effort will involve staff from the Commission's Division of Trading and Markets in cooperation with the Division of Economic and Risk Analysis.

Examples of areas that staff may evaluate include potential impacts on the national best bid and offer for equity securities and volume and quotation characteristics of exchanges with an intentional access delay. Through these efforts, or earlier as it determines, the Commission will reassess whether further action is appropriate.

As the Commission noted in its interpretation, however, markets and market participants already deal with short unintentional delays in the current system, generally as the result of geographic or technology latencies. IEX's single intentional access delay is within existing latencies experienced by market participants as they route orders between dispersed exchanges. At the same time, the importance of this issue requires careful scrutiny, and the Commission staff will gather data to inform the evaluation of any potential impact of any intentional access delays, including those established by IEX.

**Q.2.** According to some commentators, the Commission's recent approval of IEX's application to be a national securities exchange is vulnerable to court challenges.

Did you consult with the Commission's general counsel about whether the Commission's order approving IEX's application was lawful? If so, what was the conclusion?

**A.2.** Included among the responsibilities of the Office of the General Counsel is the provision of legal counsel on regulatory actions such as this one, offering explanation and analysis of open legal questions as well as legal consequences of potential Commission determinations and any associated legal risks. As part of the standard process for considering such applications, the General Counsel's office was consulted and provided its guidance to the Division and the Commissioners' offices on a range of questions and on the action that the Commission ultimately undertook.

**Q.3.** Did you consider proceeding with a rulemaking to amend Regulation NMS rather than proceeding with a de facto amendment to Regulation NMS by approving the IEX's application to allow for intentionally delayed price quotations?

**A.3.** In connection with its order granting IEX's exchange registration application, the Commission did not amend any definition or rule of Regulation NMS. Rather, in response to technological and market developments since Regulation NMS was adopted in 2005, the Commission issued an updated interpretation of the word "immediate" as used in the definition of automated quotation in Rule 600(b)(3) of Regulation NMS.

While the Commission did afford an opportunity for notice and comment by publishing a draft interpretation for comment, and did take the comments it received into consideration, it was not required to undertake a notice and comment rulemaking when updating its prior interpretation of its own regulation.

**Q.4.** The SEC's proposed rule to limit the use of derivatives in registered investment companies includes a requirement to calculate

a fund's use of derivatives based on gross notional exposure. There is concern that this form of risk measurement may lead to the unintended consequence of overweighting to certain equities and moving away from commodities markets. Commodities markets are critical for owners of actual commodities who need liquid markets. Will you commit to addressing this concern as part of the rule-making process?

**A.4.** The Commission will carefully consider all of the comment letters received as we work to finalize the proposed rule, including comment letters addressing the proposed rule's use of gross notional exposure. The proposed rule did not provide differing treatment for equity and commodity derivatives. In addition, as described in the proposing release, the Commission staff's analysis indicated that it should be possible for funds to pursue, in some form, almost all existing types of investment strategies in compliance with the proposed rule.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR HELLER  
FROM MARY JO WHITE**

**Q.1.** Shareholder voting practices have changed dramatically over the last decade. There is an increased use of proxy advisory firms to provide analysis and proxy voting recommendations. Today, two firms dominate the proxy advisory industry. In 2014, the SEC issued guidance creating oversight of proxy advisory firms for the first time.

I would like to know what activities the SEC is undertaking to ensure this guidance is being followed?

**A.1.** Since the issuance of Staff Legal Bulletin 20, SEC staff has been monitoring the changes that have been implemented by proxy advisory firms and investment advisers in response to the staff guidance.

The two largest proxy advisory firms now provide a description of their policies with regard to the disclosure of potential conflicts on their Web sites. In addition, while the Commission does not comment on specific examinations, the SEC's Office of Compliance Inspections and Examinations (OCIE) announced examination priorities for 2015, which, among other things, sought to examine select proxy advisory service firms, and how they make recommendations on proxy voting and how they disclose and mitigate potential conflicts of interest. OCIE's examination priorities for 2015 also included reviewing investment advisers' compliance with their fiduciary duty in voting proxies on behalf of investors. OCIE's efforts regarding this priority were incorporated into the ongoing Never-Before-Examined Investment Company (NBE IC) Initiative launched in April 2015. The NBE IC Initiative was conducted as focused, risk-based examinations in a number of higher-risk areas, including compliance programs. As one of the areas to be reviewed within the compliance program, OCIE announced that it would review the funds' portfolio proxy voting policies and procedures.

**Q.2.** Do you believe proxy advisory firms use sufficient resources to perform proper due diligence in their research and vote recommendations?

**A.2.** The nature and amount of resources a firm uses to perform research and make recommendations is largely a business decision of the particular firm. A proxy advisory firm provides advice to investors about securities, not unlike numerous other types of analysts and advisors in the financial markets.

As you know, some registered investment advisers may choose to retain proxy advisory firms to assist with the advisers' proxy voting duties. When considering whether to retain or continue retaining any particular proxy advisory firm to provide proxy voting recommendations, the SEC staff has stated that an adviser should ascertain, among other things, whether the proxy advisory firm has the capacity and competency to adequately analyze proxy issues, which could include, among other things, the adequacy and quality of the proxy advisory firm's staffing and personnel.

**Q.3.** How can SEC inspectors work to further ensure proxy advisory firms and their work receive proper examination, scrutiny, and is free of any conflicts of interest?

**A.3.** Proxy advisory firms that are registered investment advisers under the Investment Advisers Act of 1940 are subject to examination by OCIE. The SEC staff has historically conducted, and continues to conduct, examinations of registered investment advisers, evaluating many issues, including advisers' compliance with their fiduciary obligations and how they disclose and mitigate potential conflicts of interest.

**Q.4.** There has been several meetings conducted by the advisory committee the SEC has set up to look at equity market structures.

Do you believe that reforms to the market structures should be comprehensive and significant or do you support a small and piecemeal reform approach?

Are you satisfied with the advisory committee's results so far?

What are the current goals of the advisory committee and how and when will you complete those goals?

**A.4.** Addressing the issues of our current market structure demands a continuous and comprehensive review that integrates targeted enhancements with an expansive consideration of broader changes. In February 2015, as part of our broader market structure work, the Commission established the Equity Market Structure Advisory Committee, comprised of diverse experts to consider specific initiatives and potential structural changes. The Committee was established to assist the Commission in its comprehensive reviews of the structure of the equity markets, and I have been very pleased with the progress of the Committee's work over the past year.

The Committee as a whole has met six times to consider issues such as the operation of Regulation NMS, the impact of access fees and rebates widely used by stock exchanges, the regulatory structure of trading venues, and the impact of various market structure issues on customers. At the July meeting, the full Committee voted on recommendations from two of its subcommittees for an access fee pilot program and trading venue regulatory reforms related to NMS plan governance and self-regulatory organization proposals requiring technology changes. I expect that the staff will be considering all of these items and preparing its own recommendations for

how the Commission should take account of the Committee's work in these areas. In particular, I expect that the staff will be working to develop plans for an access fee pilot program for the Commission's consideration.

At the Committee's most recent meeting on August 2, the other two subcommittees presented their preliminary recommendations to the full Committee. Specifically, the Market Quality Subcommittee's recommendations focused on various market quality and safety features, such as limit up-limit down mechanisms and marketwide circuit breakers. The Customer Issues subcommittee focused on issues concerning retail investors, such as investor sentiment of equity market structure and modifications to Rules 605 and 606 of Regulation NMS.

Maintaining and enhancing the high quality of the U.S. equity markets is one of the Commission's most important responsibilities. The Committee's work is an important part of that and is of great assistance in our efforts to ensure that the equity markets optimally meet the needs of investors and public companies.

**Q.5.** A few months ago Senator Crapo and I held a hearing looking at changes in the fixed-income markets and looking at how regulators should work to keep the fixed-income markets open and liquid. There are early signs that fixed-income markets are becoming more fragile and less liquid than they used to be. The U.S. Treasury Department has issued a request for information from industry participants to deepen their understanding about what is happening in the fixed-income markets and the Federal Reserve is also examining this issue.

Because the mission at the SEC is to maintain fair, orderly, and efficient markets, I would like to know if the SEC recognizes the changes occurring in the fixed-income markets and do you believe that future rules and regulations should be evaluated for potential impacts on liquidity in the bond markets before implementation?

**A.5.** Commission staff actively monitors developments in the fixed-income markets, including changes in liquidity conditions, whether driven by market conditions, regulatory changes, or competitive forces. For example, in connection with implementation of the Volcker Rule, Commission staff, along with staffs of the Office of the Comptroller of the Currency, Federal Reserve Board, Federal Deposit Insurance Corporation, and the CFTC, monitors liquidity in the corporate bond market and provides quarterly reports to the House Committee on Financial Services.

Before the Commission adopts or implements any rule or regulation, the initiative is carefully considered and evaluated, taking into account public input to inform our efforts. Among other things, this process allows for market participants to identify concerns they may have about the impact on liquidity. Any potential future rules or regulations impacting the fixed income markets under the Commission's jurisdiction would be subject to a similar process and would be considered and evaluated in light of the Commission's ongoing monitoring of evolution and developments in those markets.

**RESPONSES TO WRITTEN QUESTIONS OF SENATOR SCOTT  
FROM MARY JO WHITE**

**Q.1.** Do you agree that competition among Nationally Recognized Statistical Rating Organizations (NRSROs) is important to protecting investors and that the SEC should seek to prevent entrenchment of the largest incumbent rating agencies in investor guidelines?

**A.1.** The Office of Credit Ratings, established pursuant to the Dodd-Frank Act, assists the Commission in executing its responsibility for protecting investors, promoting capital formation, and maintaining fair, orderly, and efficient markets. Congress stated that one of the objectives of the Credit Rating Agency Reform Act is to improve ratings quality by fostering competition in the credit rating agency industry, and we support Congress' objective in a number of ways. Pursuant to the Credit Rating Agency Reform Act, the staff reports on the state of competition annually as part of the Annual Report to Congress on NRSROs. As noted in the staff's December 2015 Annual Report to Congress on NRSROs,<sup>1</sup> comparing the number of ratings outstanding for established NRSROs and newer (smaller) NRSROs may not provide a comprehensive picture of the state of competition as "outstanding" ratings may not fairly reflect "new issue" rating activity. Instead, information relating to recent market share developments in the asset-backed securities rating category may provide a better gauge of how effectively newer entrants are competing with more established rating agencies. In that regard, some of the smaller NRSROs have built significant market shares in the asset-backed securities rating category, including U.S. commercial mortgage-backed securities. Additionally, some of the smaller NRSROs are rating newer asset classes, such as single-family rental securitizations and marketplace lending securitizations. With respect to preventing entrenchment of rating agencies in investor guidelines, as discussed below, to reduce investors' reliance on credit ratings, the Commission has adopted final amendments to remove references to credit ratings in approximately 30 rules or forms.

**Q.2.** Will you commit to changing Rule 2a-7 to require a reversion in investor guidelines to the term "any NRSRO"?

**A.2.** On September 16, 2015, the Commission adopted amendments to remove credit rating references in the principal rule that governs money market funds, Rule 2a-7 of the Investment Company Act of 1940, and in Form N-MFP, the form that money market funds use to report information to the Commission each month about their portfolio holdings. The amendments implemented section 939A of the Dodd-Frank Act, which requires the Commission to review its rules that require the use of an assessment of creditworthiness of a security or money market instrument and any references to or requirements in the rule regarding credit ratings, remove any reference to or requirement of reliance on credit ratings, and substitute in those rules other standards of creditworthiness that are determined as appropriate by the Commission. Under amended

<sup>1</sup>"Office Of Credit Ratings, SEC, Annual Report on Nationally Recognized Statistical Rating Organizations" (Dec. 2015), <https://www.sec.gov/ocr/reportspubs/annual-reports/2015-annual-report-on-nrsros.pdf>.

Rule 2a-7, a money market fund may invest in a security only if the fund's board of directors (or its delegate, typically the fund's adviser) determines that the security presents minimal credit risks after analyzing, to the extent appropriate, certain prescribed factors.

The amendments to Form N-MFP require a money market fund to disclose NRSRO ratings that the fund uses in its evaluations of portfolio securities. Specifically, a fund must disclose for each portfolio security any NRSRO rating that the fund's board of directors (or its delegate) considered in making its minimal credit risk determination, as well as the name of the NRSRO providing the rating. According to data submitted on Form N-MFP as of June 30, 2016, approximately 16 percent of money market funds report that they used NRSRO ratings in their credit risk evaluations of the funds' portfolio securities.

**Q.3.** What is your authority to regulate the investor guidelines of mutual funds and pension funds?

**A.3.** The Investment Company Act of 1940 (1940 Act) regulates the organization of investment companies, including mutual funds, which engage primarily in investing, reinvesting, and trading in securities, and whose securities are offered to the investing public. The 1940 Act was designed to protect investors from certain abuses and requires full and fair disclosure to the investing public of information about the fund, including about its investment objectives, financial condition, and its structure and operations, and prohibits an investment company from changing its fundamental investment policies without shareholder approval. The 1940 Act also limits funds' issuance of debt and other senior securities, and includes requirements related to valuation, redemptions of fund shares, and dealings with service providers and other affiliates. The Commission does not regulate pension funds.

**Q.4.** What other authorities does the SEC have to create a ratings environment that fosters access to the best research instead of allowing the entrenchment of incumbent NRSROs through outdated investor guidelines?

**A.4.** The Commission began removing references to credit ratings in Commission rules and forms in 2009 and accelerated that process after the enactment of section 939A of the Dodd-Frank Act. To date, the Commission has adopted final amendments to remove references to credit ratings in approximately 30 rules or forms. For example, as noted above, the Commission on September 16, 2015, adopted amendments to remove credit rating references in the principal rule that governs money market funds, Rule 2a-7 under the Investment Company Act of 1940, and Form N-MFP, the form that money market funds use to report information to the Commission each month about their portfolio holdings. In these amendments, the Commission eliminated requirements that limited money market funds to investing in securities that had received certain NRSRO ratings and instead requires that a money market fund invest only in securities that the fund's board of directors (or its delegate, typically the fund's adviser) has determined present minimal credit risks after analyzing, to the extent appropriate, certain prescribed factors.

**RESPONSES TO WRITTEN QUESTIONS OF SENATOR SASSE  
FROM MARY JO WHITE**

**Q.1.** I'd like to ask about the SEC's recent grant of exchange status to IEX.

Does the SEC expect that other exchanges will respond to the newly approved speed bump with similar innovations?

If so, how will this impact the securities market?

In approving IEX's application, the SEC issued staff guidance stating that "delays of less than a millisecond are at a de minimus level that would not impair fair and efficient access to a quotation . . ." but that some intentional delays could be "unfairly discriminatory, not an appropriate or unnecessary burden on competition, and otherwise consistent with the Act." Given this framework, how would the SEC evaluate an intentional delay that did not apply consistently and equally to all users of the exchange that implemented a delay?

Do the issues raised by IEX's successful application to become an exchange merit a review of Regulation NMS that is "comprehensive and part of formal rule making," as former SEC Commissioner Paul Atkins has called for?

**A.1.** In light of IEX's exchange registration application and technological and market developments since the adoption of Regulation NMS, the Commission decided to revisit its interpretation of the term "immediate" under Regulation NMS. The interpretation is applicable to all exchanges and provides that, solely in the context of determining whether a trading center maintains an "automated quotation" for purposes of Rule 611 of Regulation NMS, the Commission does not interpret the term "immediate" by itself to prohibit a trading center from implementing an intentional access delay that is de minimis—i.e., a delay so short as to not frustrate the purposes of the trade-through rule of Regulation NMS by impairing fair and efficient access to the exchange's quotations. While I cannot predict how other exchanges will react, the Commission's interpretation is equally applicable to them. Whether and, if so, how multiple access delays will impact the securities markets is something that the Commission's staff will monitor and consider, if such delays are ultimately implemented. The Commission's interpretation noted that a study will be completed by Commission staff within two years regarding the potential effects of intentional access delays on market quality, including price discovery.

As noted in the interpretation, any exchange that proposes to adopt an intentional access delay must do so through a rule filing of the exchange, which must be filed with the Commission and published for notice and comment by the public. Importantly, the interpretation does not change the existing requirement that, prior to being implemented, an intentional delay of any duration must be fully disclosed and codified in a written rule of the exchange that has become effective pursuant to section 19 of the Securities Exchange Act of 1934 (Exchange Act), where the exchange met its burden of articulating how the purpose, operation, and application of the delay is consistent with the Exchange Act and the rules and regulations thereunder applicable to the exchange. If the Commission cannot find that a proposed access delay is consistent with the Exchange Act, it would disapprove the proposal, rendering moot

the issue of whether a quotation with such a delay is protected. Generally, the Commission would be concerned about access delays that were imposed only on certain market participants or intentional access delays that were relieved based upon payment of certain fees.

The general issues surrounding IEX's exchange application, notably whether exchanges with intentional access delays can maintain protected quotations, has been addressed by the Commission's interpretation. Nevertheless, based on the results of the staff's study or earlier as it determines, the Commission will reassess whether further action is appropriate.

**Q.2.** I'd like to talk about the SEC's rulemaking schedule. The SEC's mission is to "protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation." Unfortunately, as former SEC Commissioner Dan Gallagher has said, "issues specific to small business capital formation too often remain on the proverbial back burner. This lack of attention doesn't just harm small business; it also harms investors and the public at large." Is there a danger that the SEC's focus on completing its various mandated rulemakings makes it difficult to fulfill its mission to facilitate capital formation?

What is the SEC currently doing to focus on the "capital formation" prong of its mission, in particular for smaller businesses?

Where are new areas that the SEC can explore to expand access to capital? For example, many have sensibly called to expand the definition of "accredited investor" to encompass sophisticated investors.

While the SEC does have an annual Government-Business Forum on Small Business Capital Formation, the SEC rarely acts on these recommendations, especially without Congressional prodding. Can you commit that the SEC will seriously evaluate every recommendation from the forum next year?

**A.2.** The Commission is deeply committed to the priority of facilitating capital formation for small businesses. The SEC's rules provide small and emerging companies with a range of options for raising capital, and it is important to assess whether those options are meeting their needs, in light of their business models and capital needs, while providing strong investor protections that promote confidence in the markets.

As I mentioned in my written testimony, the SEC has completed all of the rulemakings directed by the JOBS Act, which resulted in significant changes to the avenues for capital formation in the securities markets, especially for smaller issuers. In addition to statutorily mandated rulemakings, we also engage in discretionary rulemakings and other initiatives to promote capital formation. For example, the Commission last year issued a proposal to amend rules for smaller and intrastate securities offerings that would help facilitate State-based crowdfunding and smaller regional securities offerings by smaller companies.

Another important initiative is the pilot program to widen the minimum quoting and trading increments—or tick sizes—for stocks of some smaller companies. Following a study directed by the JOBS Act, the Commission last year approved a proposal, submitted in

response to a Commission order, by the national securities exchanges and the Financial Industry Regulatory Authority (FINRA) for a 2-year pilot program. The SEC plans to use the pilot program to assess whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors. The pilot is scheduled to begin on October 3, 2016.

We are committed to our mission of facilitating capital formation for all businesses, large and small, and we understand it is particularly important to hear the views of small business owners, investors, and other stakeholders in the small and emerging business community. As you note, the SEC hosts an annual forum focusing on small business capital formation, called the Government-Business Forum on Small Business Capital Formation (Small Business Forum). This forum has assembled annually since 1982, as mandated by the Small Business Investment Incentive Act of 1980, and provides a platform to highlight concerns related to small business capital formation and to consider the ways in which these concerns can be addressed. Every year, the Small Business Forum seeks to develop recommendations for Government and private action to facilitate small business capital formation.

Further, twice during my time as Chair, the SEC has renewed the charter for its Advisory Committee on Small and Emerging Companies (ACSEC). The ACSEC includes expert members from across the small business spectrum and provides the SEC with valuable recommendations and input. Pursuant to its charter, the ACSEC provides advice on our rules, regulations, and policies as they relate to:

- capital raising by emerging privately held small businesses and publicly traded companies with less than \$250 million in public market capitalization through securities offerings, including private and limited offerings and initial and other public offerings;
- trading in the securities of emerging companies and smaller public companies; and
- public reporting and corporate governance requirements of emerging companies and smaller public companies.

Both the Small Business Forum and the ACSEC help ensure that the views of small businesses, investors, and other stakeholders in this community are clearly heard here at the SEC, and their recommendations are considered thoroughly. For example, we recently proposed amendments to the “smaller reporting company” definition that would expand the number of companies that qualify as smaller reporting companies, thus enabling them to provide certain existing scaled disclosures under Regulation S-K and Regulation S-X. This change was a recommendation of both the Small Business Forum and the ACSEC.

You also asked about the “accredited investor” definition. In another important step for modernizing the private offering market, the SEC published a staff report in December 2015 regarding this definition. The report analyzes various approaches for modifying the accredited investor definition and provides staff recommendations for potential updates and modifications. The report recommends that the SEC consider additional measures of sophistica-

tion for individuals to qualify as accredited investors (other than looking solely at income and net worth). The report also evaluates the impact that potential changes to the definition would have on the size of the accredited investor pool.

In July 2016, the ACSEC provided recommendations to the SEC regarding the accredited investor definition. I have directed the staff to prepare recommendations for the SEC on whether and how the definition should be modified, and the recommendations provided by the ACSEC and the SEC's Investor Advisory Committee, as well as all of the comments we are receiving in response to the report, will help inform the next steps.

In addition to our rulemaking initiatives and our continued engagement with the Small Business Forum and ACSEC and their respective recommendations, SEC staff routinely engages with the public and companies on questions of small business capital formation. For example, staff in the Division of Corporation Finance's Office of Small Business Policy answers questions from market participants on a daily basis about disclosure and other issues relating to smaller public companies and about limited, private, and intrastate offerings of securities. This exchange is an important part of the work we do on behalf of investors and issuers involved in smaller businesses.

**Q.3.** I'd like to discuss the marketplace online lending ecosystem, which has grown significantly as of late.

My understanding is that SEC regulations require online marketplace lenders such as Prosper and Lending Tree to update their regulatory filings with the SEC every week or so. Do you believe this is the most effective way to regulate these companies?

**A.3.** The Federal securities laws are designed to protect investors in connection with the offer and sale of securities. Those investor protections include disclosure requirements and antifraud provisions that hold companies responsible for providing false or misleading information to investors.

Obtaining money from investors to fund borrower loans through an online lending platform involves the offer and sale of securities. These offers and sales are subject to the same registration provisions of, and can take advantage of the same exemptive provisions from, the Securities Act of 1933 as any other company engaging in an offering of their securities, including "brick and mortar" lenders. The requirements for updating the information provided to investors is the same as those for other companies engaged in the offer and sale of securities.

Commission staff has worked with online marketplace lenders to help them meet registration and disclosure requirements. For example, staff in the Division of Corporation Finance consulted with online marketplace lenders as they crafted a structure to fund loans and sell notes in a manner compliant with the Federal securities laws. As with other companies engaging in continuous registered offerings of securities under the Federal securities laws, these companies have an obligation to provide disclosure to investors about the securities being acquired.

**Q.4.** Is the SEC exploring alternative means of regulating online marketplace lenders that do not involve such a robust filing re-

quirement? Would any of these changes require statutory authorization?

**A.4.** The Commission and the Federal securities laws provide a number of ways companies can raise capital, with different disclosure and reporting standards depending on who they sell to and how much they raise. To date, the need for an alternative system to regulate online marketplace lenders is not apparent based on the practices we have observed in the industry.

When marketplace lenders seek to access the public capital markets, as with any other company, they must comply with the registration and disclosure requirements of the Federal securities laws. I believe that investors need certain disclosures, including about the risk of loss of all principal and interest upon a borrower's default, to make an informed investment decision.

**Q.5.** Would there be merit to creating a broad safe harbor for marketplace online lenders which scales registration requirements to reflect their unique business model?

**A.5.** I believe the Federal securities laws provide a number of options already, and it is not clear to me at this time that the business model of marketplace lenders would merit its own registration regime. Marketplace lenders are currently able to raise capital in private and public markets.

**Q.6.** Some have criticized the SEC's treatment of machine-readable, open data, including for its implementation of a dual-filing requirement for both XBRL and old fashioned documents, and a slow transition toward allowing the filing of inline XBRL, which is both human-readable and machine-readable. In addition to this step, how does the SEC plan to modernize its treatment of Government data and transition toward open-data?

**A.6.** The Commission has a longstanding commitment to using developments in technology and electronic data communications to facilitate easier access to information. Machine-readable financial market data enhances our rulemaking and market-monitoring activities and makes disclosures more usable for the public.

What to disclose, and how to disclose it, are vital questions that we ask in any rulemaking that involves the reporting of information to the Commission. Thus, in several recent rulemakings, the Commission has either proposed or adopted disclosures that would be made in a structured format. For example, in adopting Regulation Crowdfunding, the Commission required Form C (containing issuer disclosures) to be filed in eXtensible Markup Language (XML). Similarly, the final rule amendments to Regulation AB required asset-level disclosures in XML. In addition, in the recently issued Regulation S-K concept release, the Commission specifically sought comment on whether to require registrants to provide additional disclosures in a structured format.

I am also committed to exploring other ways to enhance the availability and usability of structured data. For example, staff has posted on the Commission's Web site reformatted financial information that was reported by companies in their filings in XBRL format. Specifically, staff has combined and organized as-reported XBRL data into structured file sets to facilitate improved data analysis by the public.

Finally, in addition to promoting the public availability and usability of structured data, the SEC has been proactively incorporating structured data into its own internal processes. Structured data enhances our rulemaking and market-monitoring activities; for example, it is a valuable input into several risk assessment tools that our Division of Economic and Risk Analysis, Division of Enforcement, and Office of Compliance Inspections and Examinations have been jointly developing and deploying to enhance the effectiveness of Commission staff in detecting wrongdoing.

**Q.7.** Australia has created a Standard Business Reporting regime (SBR) that allows a company to complete one filing to comply with multiple regulatory disclosure requirements. This has extensively reduced the amount of required data fields, saving the Australian economy more than \$1 billion annually by one estimate. Could a similar regulatory regime be possible in the United States? Have you discussed this possibility with other regulators?

**A.7.** It is my understanding that Standard Business Reporting (SBR) is an Australian Government initiative that was introduced in 2010 to simplify the business reporting obligations of companies that report to the Australian Government. SBR uses standard terms that are built into software technologies to facilitate the dissemination of business and accounting information across participating Government agencies. While it may be possible to implement a similar regulatory regime among regulatory authorities in the United States, such a regime likely would involve significant planning and close coordination among various regulatory agencies with different missions and priorities and may require statutory changes to implement. I have not discussed this possibility with fellow regulators.

The SEC's disclosure rules require companies that offer and sell securities to the public and that are required to file periodic reports with the Commission to provide information about their business and financial condition, among other things. The staff of the Division of Corporation Finance is engaged in a broad-based review of our disclosure rules to determine how we can make our requirements more effective for investors and companies. The Commission has issued releases resulting from this review on a variety of topics, including a concept release on business and financial disclosures required by Regulation S-K. Among the topics addressed in the concept release is the use of data tagging to facilitate disclosure and review of information. The staff is currently considering the comments received on the concept release.

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#### **RESPONSES TO WRITTEN QUESTIONS OF SENATOR ROUNDS FROM MARY JO WHITE**

**Q.1.** Are you concerned by the fact that issuance of private stock has now outstripped public shares sold to all retail investors, in terms of new issuance? He asked this question during the hearing but would like to follow up with QFRs on the same topic with the following two questions.

What are the long term implications of this shift?

What if anything is the SEC doing about this trend, to try to stimulate IPOs?

**A.1.** As you note, in recent years, the size of the private capital raising market in terms of the total number of offerings conducted and dollar amounts raised has outpaced the size of registered securities offerings. While the long term implications of the current trend are not entirely clear, it is the responsibility of the Commission to ensure that investors are protected, whether in public or private markets, and that issuers have a range of means to raise the capital they need to fuel their businesses.

Specifically, a robust private capital raising market must provide all investors—irrespective of their income or net worth—with investment opportunities and strong investor protections. In implementing its JOBS Act mandates, the SEC created new and revitalized existing exemptions for capital raising options for companies and investment opportunities for investors, including rules that allow companies to generally solicit investors in certain private offerings, conduct securities-based crowdfunding offerings, and raise capital pursuant to an updated and expanded Regulation A. The fact that companies are increasingly relying on these and other avenues for capital is consistent with our goal of promoting capital formation by providing issuers a diverse range of capital-raising mechanisms backed with strong investor protections.

In addition to creating new avenues for capital formation, the JOBS Act included provisions that created a new category of companies in registered offerings, called “emerging growth companies” (EGCs). These provisions provided a number of accommodations for companies that qualify as EGCs.

Since enactment of the JOBS Act, SEC staff has issued detailed guidance on the EGC-related provisions and procedures to assist companies in navigating the so-called IPO on-ramp. To date, the SEC has received over 1,100 confidential submissions of draft registration statements by EGCs seeking to conduct a registered initial public offering.

Having an effective disclosure regime is critical for capital formation and investor protection. In late 2013, based in part on the results of a JOBS Act mandated report on the disclosure requirements for companies included in Regulation S-K, I directed SEC staff to develop specific recommendations for updating our rules that dictate what a company must disclose in its filings. The overall goal of the disclosure effectiveness initiative is to comprehensively review our disclosure requirements and to make recommendations to update those requirements to make disclosure more meaningful, accessible, and efficient for investors. Last year, as part of this review, the SEC published a request for comment on what investors, companies, and market participants would like to see with respect to the form and content of financial statement disclosures by entities other than the registrant under Regulation S-X. Additionally, this year as part of the disclosure effectiveness initiative, as well as to facilitate implementation of the Fixing America’s Surface Transportation (FAST) Act, the SEC issued a broad-based concept release seeking input from investors, issuers, and other affected market participants on our business and financial disclosure requirements, proposed rules to modernize the SEC’s disclosure requirements and policies for mining properties, and, most recently, proposed amendments to address outdated and re-

dundant disclosure requirements while continuing to require companies to provide investors with the information they need to make informed decisions.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARNER  
FROM MARY JO WHITE**

**Q.1.** Chair White, last year, NASDAQ and NYSE filed petitions for rulemaking asking the SEC to promulgate rules to increase transparency around short selling. Other groups supported those petitions as well. While short selling can be important for liquidity and hedging, it is also important to ensure an equitable disclosure regime for short and long investors. As you know, there is currently more disclosure required for long positions.

Can you please comment on the status of these petitions? Does the SEC plan to act on this issue?

**A.1.** Extensive short sale data is currently publicly available, free or on a fee basis, including daily short sale volume and transaction data, short interest data, and fails to deliver data. The Commission staff has worked with the self-regulatory organizations (SROs) to make short sale data available to the public, including aggregate daily short selling volume in individual equity securities; on a 1-month delayed basis, information regarding individual short sale transactions in exchange-listed equity securities; and semimonthly statistics on short interest. The Commission also publishes on its web site “fail-to-deliver” information semimonthly for all equity securities.

I am committed to ensuring that short sale data strikes the right balance between disclosures necessary to protect investors while preserving the benefits of price discovery and liquidity that short selling can bring to the market. In comparing disclosure regimes for short and long investors, it is important to consider the different purposes that such requirements would seek to address. Most notably, public disclosure of long positions provides information regarding persons that may have potential influence over, or control of, the issuer. Similar disclosure of short positions would not provide such information.

The Commission staff continues to consider, as part of Dodd-Frank Act section 929X and in conjunction with the June 2014 staff study of real-time short sale disclosure required by the Dodd-Frank Act, whether additional transparency may be warranted. In that context, the Commission staff also takes into account feedback from all market participants, including the petitions from NASDAQ and NYSE.

**Q.2.** Over the past few years, investors and market participants have experienced disruptions in the timely dissemination of public market data via the Securities Information Processors or SIPs, operated by various exchanges, including at NASDAQ in 2013. After the NASDAQ glitch, which shut down trading on NASDAQ listed stocks for three hours, you convened a meeting with exchange CEOs to discuss how to improve resiliency. These same entities sit on the governance committee overseeing our current market structure. Yet SIP outages affect the entire stock and options markets, and so it seems to me that entities who must make the decisions

about whether or not to invest in the public data feeds and make necessary improvements to vital market infrastructure ought to not be the only voice in the room. While the current set of recommendations may be insufficient, the Equity Market Structure Advisory Committee has recommended changes to the governance structure. Would you agree that it is time to update the governance structure for NMS Plans and the operating committee?

**A.2.** NMS plan governance is one of the many important topics the Commission currently is assessing as part of its broad-based review of equity market structure. For example, the Equity Market Structure Advisory Committee at its July 8, 2016, meeting recently made a number of recommendations to the Commission relating to trading venues regulation.<sup>1</sup> Those recommendations include expanding the role of NMS plan advisory committees to provide them with a formal vote on any matter on which the operating committee votes, as well as to initiate their own recommendations to the operating committee, so as to make NMS plan advisory committees more significant, formalized, and uniform.<sup>2</sup> I expect the Commission will give these recommendations full consideration as it considers governance structure changes in NMS plans.

As we assess possible changes to the governance structure for NMS plans, it is important to bear in mind that such plans serve important regulatory purposes, such as ensuring that accurate and reliable consolidated market data is widely available to investors, that our markets have robust mechanisms to protect against excessive volatility, and that SROs can effectively surveil the markets. At the same time, I recognize the importance of incorporating the views of broker-dealers and other stakeholders in the operation of an NMS plan at an early stage of the decision-making process. Early-stage engagement may, among other things, enhance the quality of the proposals developed by the NMS plans as well as facilitate more swift adoption and implementation. Accordingly, enhancements to the governance of NMS plans designed to ensure that the views of key stakeholders are taken into account are among the significant issues under consideration.

**Q.3.** Chair White, you previously announced as part of the Regulatory Flexibility agenda for the Spring of 2016 that a potential rulemaking to shorten the settlement time for securities would be complete by the end of June of this year. Can you please give me an update on the status of this rulemaking?

**A.3.** I and my fellow Commissioners have publicly stated our support for efforts to shorten the settlement cycle from the third business day after the trade date to no later than the second business day (T+2). Shortening the settlement cycle should yield important benefits, including reduced counterparty risk, decreased clearing capital requirements, reduced procyclical margin and liquidity demands, and increased global harmonization. While current SEC rules do not prevent the implementation of T+2, updates to those rules could help support the move to T+2 by all market partici-

<sup>1</sup> The recommendations can be found at the Equity Market Structure Advisory Committee's spotlight page. See "Equity Market Structure Advisory Committee Telephone Meeting", SEC.gov (July 8, 2016), [https://www.sec.gov/video/webcast-archive-player.shtml?document\\_id=070816emsac](https://www.sec.gov/video/webcast-archive-player.shtml?document_id=070816emsac).

<sup>2</sup> See id.

pants, as well as to shorter settlement cycles potentially in the future. I therefore have instructed Commission staff to develop a proposal to amend SEC Rule 15c6-1(a) to require settlement no later than T+2 for Commission consideration this year. In developing the proposal, Commission staff has been working with various market participants regarding the key issues surrounding shortening the settlement cycle to T+2. I expect that the proposal will be published in the fall of this year.

While this initiative complements the work of the securities industry and the SROs, it should not be seen as a precondition or an impediment to the ongoing industry progress to shorten the settlement cycle. There has been a tremendous amount of work done to date by a broad range of market participants toward achieving the transition to T+2, and this effort must continue expeditiously to completion.

**Q.4.** On July 21, 2015, Sen. Mike Crapo and I wrote to you to ask when the Commission would fix its duplicative requirement for public companies to file two versions of every financial statement—first as a document, then the same information again in the XBRL open data format. We pointed out that collecting two versions (1) distracted Commission staff from enforcing the quality of the data version; (2) delayed the broader modernization of the Commission’s whole corporate disclosure system from document-focused to data-centric; and (3) imposed unnecessary costs on public companies, who must check the two versions against each other. On August 19, 2015, you responded that the Commission staff were “developing recommendations to allow filers to submit XBRL data inline as part of their core filings.” I was pleased to see that just last week, June 13, the Commission issued an order allowing (but not requiring) public companies to file a single version of their financial statements, using the inline XBRL format, which is both human-readable and machine-readable. The order expires in March 2020. What do you expect the Commission will learn from this temporary period of voluntary inline XBRL filing?

**A.4.** I believe that inline XBRL has the potential to provide a number of benefits to filers and users of structured financial information. For example, inline XBRL could decrease filing preparation costs, improve the quality of structured data, and, by improving data quality, increase the use of XBRL data by investors and other market participants.

As the Commission’s exemptive order noted, permitting the voluntary use of inline XBRL allows the Commission to further assess the usefulness of inline XBRL and can facilitate further development of inline XBRL preparation and analysis tools, provide investors and companies with the opportunity to evaluate its usefulness, and help inform any future Commission rulemaking in this area.

Additionally, a voluntary period of inline XBRL filing can allow the Commission to review and evaluate whether our beliefs regarding the potential benefits of inline XBRL are correct. It can also provide us with additional input to inform our consideration of whether to adopt a mandatory rule and, if so, whether the rule should include certain exemptions or phase-in provisions. A voluntary filing period can also provide an opportunity for any techno-

logical or practical issues associated with inline XBRL to be identified and resolved prior to potentially requiring the use of inline XBRL.

**Q.5.** Although I am pleased to see that the Commission has finally announced a pathway toward full open data for corporate financial statements, I am disappointed that the Commission did not publish the data structure (known as a specification) for inline XBRL filing in advance, to give public companies, disclosure management software providers, data consumers and other stakeholders a chance to review and comment on it. Instead, the Commission published the specification and issued the order simultaneously, leaving public companies and software providers scrambling to review the specification, and creating a delay before inline XBRL filing can begin and uncertainty about the impact of this change on data consumption.

This failure to publish a data structure in advance of the legal order contrasts with the approach taken by the Treasury Department in implementing the DATA Act of 2014, which I introduced in the Senate and which requires the Federal Government to adopt a standardized open data structure for its own financial information. The DATA Act requires standardized financial reporting by Federal agencies to begin in May 2017, but the Treasury Department has already published several versions of the data structure for review and comment by agencies, software firms serving them, and other interested parties.

For future changes to the data structures it uses to collect securities disclosures, will the Commission commit to publishing such data structures at least 60 days in advance of any legal order permitting or mandating their use?

**A.5.** The Commission seeks to provide the public with adequate notice regarding technical implementation issues associated with structured data. For example, when the Commission in December 2015 proposed a new rule specifying the form and manner with which security-based swap data repositories (SDRs) will be required to make security-based swap data available to the Commission—specifically, requiring SDRs to make data available using schemas published on the Commission’s Web site and referencing international industry standards Financial products Markup Language (FpML) and Financial Information eXchange Markup Language (FIXML)—the Commission also posted for public comment the related technical schemas. Similarly, draft copies of amendments to the EDGAR Filer Manual are generally posted on the Commission’s Web site in advance of Commission approval to help filers, agents, and software developers prepare for potential technical changes related to filing on EDGAR. More generally, Commission staff proactively engages with the software and services vendor community, inquiring about their capabilities and readiness with respect to various matters that the Commission has indicated an interest in potentially pursuing, such as inline XBRL, the IFRS taxonomy, or structuring of data outside the financial statements.

With respect to the inline XBRL exemptive order, the Commission was permitting voluntary implementation, rather than requiring compliance by a date certain. One of the objectives of this vol-

untary filing program is to provide investors, preparers, and third party service providers a means to assess the technical requirements and provide feedback to staff during the voluntary period, in advance of any determination whether to require issuers to file using Inline XBRL. Delaying effectiveness of the exemptive order to provide advance notice of the technical requirements would have impeded issuers and preparers from voluntarily participating in the program and providing valuable feedback when ready. In this regard, I note that the first inline XBRL filing was submitted to the Commission on July 1, three weeks after the exemptive order was issued.

**Q.6.** Financial statements are filed as part of larger periodic filings under the Exchange Act of 1934. Forms 10-K and 10-Q include a great deal of information beyond the financial statements that today is expressed in plain-text document form, not open data. For example, Exhibit 21 to the 10-K requires a public company to identify its subsidiaries. This list of subsidiaries is plain text, not electronic data fields, which makes it very difficult for investors' software to automatically identify a company's subsidiaries and link them to other databases. But by adopting inline XBRL, the Commission is opening an easy avenue to transform more of the periodic filings from plain text into open data. Companies will be filing each Form 10-K and 10-Q as a single human-readable HTML document with embedded electronic tags that identify particular data fields. At first, only the financial statements will be tagged, but the Commission could add new tags to information such as Exhibit 21 to make such information electronically searchable as open data. Do you expect that the adoption of the inline XBRL approach for financial statements will start a broader modernization of the Exchange Act filings, with electronic tags being added for other types of information contained in them?

**A.6.** What to disclose, and how to disclose it, are vital questions that the Commission must ask in any rulemaking that involves the reporting of information to the Commission. Thus, in several recent rulemakings, the Commission has either proposed or adopted disclosures that would be made in a structured format. For example, in Regulation Crowdfunding, the Commission required Form C (containing certain issuer disclosures) to be filed in eXtensible Markup Language (XML). Similarly, the final rule amendments to Regulation AB required asset-level disclosures in XML. In addition, a number of recently proposed rules also have included structured information, including those on executive compensation and enhanced reporting by investment companies.

In addition, the Commission has been considering whether to extend structuring requirements in its existing rules. In the recently issued Regulation S-K concept release, the Commission specifically sought comment on whether to require registrants to provide additional disclosures in a structured format, including whether there are categories of information in Parts I and II of Form 10-K or in Form 10-Q that investors would want to receive as structured data. We look forward to input from commenters to help us assess investor interest in the structuring of existing disclosures outside the financial statements.

**RESPONSES TO WRITTEN QUESTIONS OF SENATOR MERKLEY  
FROM MARY JO WHITE**

**Q.1.** I am very concerned that the SEC, under your leadership, has dropped the issue of political spending from its agenda.

When it comes to spending on political activity, only roughly 2.2 percent of all public companies in the United States make such disclosures voluntarily.<sup>1</sup> There's been a dramatic increase in spending by corporations that do not disclose their donors in recent years from less than \$5.2 million in 2006 to over \$300 million in the 2012 Presidential election cycle.

As you mentioned in the hearing, 50 percent of the S&P 500 companies disclose their political spending voluntarily. However, in a cursory glance of a handful of those companies, the disclosure of this type of spending varies widely. Some public companies disclose the topline information about a company's policy and political priorities while others list specific amounts donated for races that range from candidates running for President to officials at the State and local level.

In 2012, included on the Regulatory Plan and Unified Agenda, in a Proposed Rule State, was "the Disclosure Regarding the Use of Corporate Resources for Political Activities."

In the Spring 2013, consideration of the political disclosure rule was missing from the Update to the Unified Agenda. Instead, the agenda item had been relegated to the list of Spring 2013 Long Term Actions. This move coincided with your arrival at the SEC.

In the Fall of 2013, the political disclosure rule was omitted altogether from both the Unified Agenda as well as the Long Term Actions. This omission was several months into your first year as SEC Chair.

Considering the timeline, it is difficult not to draw a line directly from the start of your time at the SEC to the eventual dismissal of a political spending disclosure rule.

While the political spending disclosure rule is no longer on the SEC's agenda for consideration, many Americans believe it should be. To date, more than 1.2 million securities experts, individual and institutional investors, ranging from former SEC Chairs Levitt and Donaldson and SEC Commissioners to mutual funds and State Treasurers as well as members of the public have pressed the SEC for a rule that would require public companies to disclose this very material information. In addition, 44 Senators wrote in support of the petition to the SEC to take up the political disclosure rule.

Former SEC Commissioner Luis Aguilar in a 2012 speech said that shareholders of corporations are "often in the dark as to whether the companies they own, or contemplate owning, are making political expenditures. Withholding information from shareholders is a fundamental deprivation that undermines the securities regulatory framework which requires investors receive adequate and appropriate information, so that they can make informed decisions about whether to purchase, hold, or sell shares—and how to exercise their voting rights."

<sup>1</sup> Calculation made using number of public companies that disclose corporate political spending divided by total number of public companies. Dan Strumpf, "U.S. Public Companies Rise Again", *The Wall Street Journal*, Markets, 5 February 2014, <http://www.wsj.com/articles/SB10001424052702304851104579363272107177430>.

The founder of the largest provider of mutual funds, Vanguard's John C. Bogle, said, "It's high time that the abuse of corporate political spending comes to an end. Disclosure of corporate political contributions to the corporation's shareholders—its owners—is the first step toward dealing with the potentially corrupt relationship between corporate managers and legislators. Shareholders must not be left in the dark while their money is spent without their knowledge."

As Chair of the SEC, do you believe that shareholders, as owners of the company, have the right to know about the corporation's spending for political purposes?

Do you believe this information is material to investors? If not, why not?

**A.1.** The subject of corporate political spending (and requiring its disclosure) is an important one on which there are strong and differing views. There is no specific statutory or rule-based disclosure requirement under the Federal securities laws or other Federal law mandating that public companies disclose information relating to their political contributions. While there is no specific mandate under existing law, if a company's corporate political spending has a material impact on its results of operations or financial condition (or if omission of disclosure on this subject would make other disclosure included in a filing materially misleading), disclosure to shareholders by the company is required.

In addition, under the Commission's Rule 14a-8, a shareholder may submit a proposal for inclusion in its company's proxy materials seeking disclosure or other action on political contributions. This avenue has been used by a number of shareholders, with such proposals in 2016 averaging support of 26.1 percent of votes cast.<sup>2</sup>

As I noted during the hearing, a number of other public companies have also made voluntary disclosures of their political spending. For example, a 2015 Center for Political Accountability report found that 87 percent of companies in the S&P 500 have adopted policies addressing political spending, 54 percent of S&P 500 companies have a dedicated web page or similar space on their Web site for political spending disclosure, and 43 percent of S&P 500 companies have board oversight of their political contributions and expenditures.<sup>3</sup> Further, the study noted that in 2015, 52 percent of S&P 500 companies had a detailed policy on their Web sites governing political expenditures with corporate funds, and 60 percent of S&P 500 companies provided information on which political entities they will or won't give money to. These avenues of engagement are important and to be encouraged, and I will continue to follow them closely.

As you know, the Consolidated Appropriations Act of 2016 prohibits the Commission from using any funds made available by the Act to finalize, issue, or implement any rule, regulation, or order regarding the disclosure of political contributions, contributions to

<sup>2</sup>See Gibson Dunn, "Shareholder Proposal Developments During the 2016 Proxy Season" (June 28, 2016), <http://www.gibsondunn.com/publications/Documents/Shareholder-Proposal-Developments-2016-Proxy-Season.pdf>.

<sup>3</sup>See Center for Political Accountability, "The 2015 CPA-Zicklin Index of Corporate Political Disclosure and Accountability" (Oct. 8, 2015), [http://files.politicalaccountability.net/index/CPA-Zicklin\\_Index\\_Final\\_with\\_links.pdf](http://files.politicalaccountability.net/index/CPA-Zicklin_Index_Final_with_links.pdf).

tax exempt organizations, or dues paid to trade associations. I have not committed, and do not plan to commit, staff resources in FY16 to develop a rule regarding disclosure of political contributions as encompassed by the Appropriations Act prohibitions.